The Growth of Credit Unions and Credit Co-operatives – Is The Past Still Present?

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Financial exclusion and the co-operative revival

Toxteth is an inner-city area of Liverpool. Over 38% of the population are unemployed and most people struggle to make ends meet either on welfare benefits or on low incomes. Like 4.4 million other people in Britain[1], most people in Toxteth live on the margins of financial services provision. Yet, as in many other similar places, most banks no longer find it profitable to preserve an effective local service. Three banks have closed their Toxteth branches over the last ten years. The one remaining bank is, in 1999, reducing its service from five to just three days a week. Whilst people elsewhere take for granted the use of cash machines, credit cards and a range of banking facilities, people in Toxteth find themselves increasingly excluded from any form of affordable financial service. Banks, they believe, are neither interested in them nor appropriate to their needs. Indeed, many people do not have a bank account. Not a small number are forced into the hands of extortionate finance companies.

In the mid-eighties, a group of people came together in Toxteth. Like the Rochdale pioneers of the nineteenth century, they shared a common belief in the ability of their community to respond collectively to its own social and economic needs. They were convinced that the only way that Toxteth would have a decent financial service was if the people of Toxteth created it for themselves. Inspired by a renewed spirit of co-operation, this group of about 25 volunteers, most of whom were women, trained together and worked to mobilise the support of a network of local community organisations. In February 1989, the group opened their own financial co-operative and the Park Road Community Credit Union was born. In 1999, this credit union has 1,700 adult and 500 junior members. It has assets of £304,000, members' savings of £254,000 and, in the financial year 1997-98, made loans to its members of £270,000. The credit union is still run by a team of 60 local volunteers. It operates from a tiny two-bedroomed terraced house in a typical Liverpudlian street. Yet it has gone some way to achieve what many of the banks in the area could not do. It has enabled its members, all local residents, 68% of which live on welfare benefits, to access an affordable financial service able to respond to their own needs and circumstances. Park Road is just one of a growing number of British credit unions that are proving to be part of the answer to present-day social and financial exclusion.

Credit unions – a modern movement founded on nineteenth century principles

Credit unions are not-for-profit, financial co-operatives that offer low-cost financial services to their members. They are based on international co-operative and democratic principles which have remained essentially unchanged since the days of the co-operative pioneers of the nineteenth century. The first known credit union was set up in Heddesdorf, Germany in 1869. Since then, they have developed in two distinct but related directions. In most European countries, they became the European co-operative banks. These are now dominant consumer financial providers that serve the general public. In North America, a different model of financial co-operative enterprise took hold. Using, for the most part, the name "credit union", these member co-operatives have a much more local and autonomous structure than their European cousins. They are based on a strong notion of a common bond, understood as a relationship that defines a certain unity between the members. Membership of a credit union is, in fact, restricted to people who share the common bond. This is, determined, usually, as either living or working in a particular locality, being employed by a particular employer, following a particular occupation or being a member of an association or society. Credit unions, as known in Britain, Ireland and Eastern Europe, developed out this North American model.

Credit unions are found in 87 countries throughout the world. Between them, these credit unions have some

85 million members. In Europe, they are strongest in Ireland, where around 44 per cent of the population are members of more than 550 credit unions. Collectively, these credit unions have more than IR£2.6 billion in assets. In Central and Eastern Europe, the credit union movement is growing fast. In Poland, for example, in just four years, 220 credit unions have been established, serving almost 260,000 members and having assets amounting to $158 million (US). Already credit unions are the fourth largest financial service provider network in the country. Similarly in the Czech Republic, in March 1999, there were 77 credit unions with over 70,880 members. Credit union movements have also been established in Russia, Romania, the Ukraine, Latvia and Lithuania and are emerging in Albania, Slovakia, Macedonia and Georgia. In fact, the largest credit unions in Europe are the US-based credit unions serving the US military and United Nations organisations. The US Navy Federal Credit Union, for example, has 1.8 million members world-wide and operates from bases in Italy, Spain, Greece and the United Kingdom.

There have been credit unions in Britain since 1964. However, the greatest rise in the number of credit unions has been over the last ten to fifteen years. In 1985, there were just 64 credit unions in Britain, in 1999 there are over 600 with over £118 million in assets and around 216,000 members. Overall, there has been two main strands to British credit union development. First, as in Toxteth, groups of local people have come together, in predominantly low-income areas, to set up their own community credit unions. The second strand of development has been amongst groups of workers in a particular profession, company or organisation. Some of the largest credit unions in Britain are organised by employees in local government or working for the police force, for bus companies, as taxi drivers or for British Airways. The largest work-based credit union in Britain is, for example, Glasgow Council Credit Union in Scotland serving employees working for the municipal authority. It has over 10,000 members and over £11 million in assets.

Co-operation - the best approach to tackling local social and economic needs?

Wherever they occur, co-operative credit unions arise in response to both social and economic needs. In nineteenth century Europe, the first credit unions were created to alleviate the hardships associated with the growth of modern capitalist economies. In the early twentieth century, credit unions in the United States, as described by Hannon, West and Barron[2], were pioneered very much as a grass-roots social movement aimed at enabling working people to obtain credit at reasonable rates. The ideology and rhetoric of the early US movement was often a crusade against loan sharks and moneylenders. Similarly, Ferguson and McKillop[3] explain the development of Irish credit union movement as a direct response to the high unemployment, the high interest rates, and the growth of illegal money-lenders that were symptomatic of the economic depression suffered in Ireland in the early 1950's.

In Britain, it was the social inequality and deprivation, faced by many communities through the eighties and nineties, that encouraged many local groups to set up credit unions. As Oppenheim and Harker point out[4], in 1992, 33% of the British population were living in or on the margins of poverty. People in this situation inevitably faced increasing financial exclusion from mainstream banks and financial institutions. Banks were just not keen to attract people in poverty as customers. It was no coincidence that it was at this time that the registration of community credit unions expanded significantly. Similarly, the rising costs of mainstream banking services led groups of workers to set up credit unions that would offer them both easier access to low-cost loans and possible higher dividends on savings. Similar developments were replicated in Central and Eastern Europe where the social and economic situation since the collapse of communism, and the resultant lack of confidence in banking services, has stimulated the opening of credit unions.

Credit unions offer an important opportunity for people to work closely together for their own mutual benefit. There is no evidence that the profit-maximising and investor-owned banking sector has either the interest or capability to respond to the needs of financially excluded and low-income groups within society. In certain circumstances, co-operative enterprise may offer the best approach to meeting the social and economic needs of particular communities. According to Fischer[5], in accessing those segments of the market which are unattractive to mainstream banking institutions, credit unions have a competitive edge insofar as the presence of a common bond generates a certain trust between the members of the organisation.

This trust offers credit unions real benefits in limiting the problems of gathering information, of transaction costs and of risk. It means that, in certain circumstances, credit unions have the potential to offer a much more efficient and cost-effective service to low income groups than either banks or other financial institutions. Clearly, a significant factor here is ownership. Credit unions are often able to access people and communities in ways inaccessible to banks as they are owned and controlled by those people and communities themselves. Hargreaves[6] stresses this point when he writes, *"the issue of ownership lies at the very heart of social exclusion"*. Capitalist enterprises have no problem in recognising the value of promoting employee share ownership schemes in order to generate a sense of ownership among their workers. Credit unions are able to generate a similar sense of ownership among the financially excluded and thus enable them to avail themselves of financial services appropriate to their needs. In Britain, the potential of credit unions is increasingly recognised by the Government, by municipal authorities and by other major agencies. Credit unions are regarded by them as being best placed, within the financial services industry, to provide low-cost financial services to those on low incomes or to those who have no access to affordable banking services. In fact, the British Government has proposed that credit unions play a key role in tackling financial exclusion. Equally, many municipal authorities see credit unions as essential contributors to the social and economic regeneration of their areas.

The British experience – the challenge of providing a professional service

Faced with the challenge of adopting a much more high-profile role in financial service provision, the British credit union movement has had to face up to a concern that has been troubling many credit union activists for some time. This concern is that many, particularly community, credit unions are not growing as significantly as they are, for example, in Ireland or in Poland. Consequently, their potential to make a difference within their communities is not being fully realised. With some exceptions, the average membership of British community credit unions does not exceed 200 members even after many years of development. Many of these credit unions are also financially very weak. Yet, at the same time, many work-based and some community credit unions are sustaining substantial growth and making a real impact among groups of workers or within communities. Undoubtedly, the highest growth rates are found in work-based credit unions. These make up just 15% of the total number of credit unions in Britain, but account for 50% of all credit union members and hold 70% of all credit union assets. Nevertheless, among community credit unions, there are examples of medium and high growth enterprises. Among these are Park Road Credit Union, in Toxteth, mentioned above, and Dalmuir Credit Union in Clydebank, Scotland. This latter credit union has, in 1998, around 5500 members, 50% of which are identified as unemployed or unwaged, and over £3 million in assets.

In endeavouring to create a financial co-operative movement that is able to respond to the needs of a much wider population, the Association of British Credit Unions (ABCUL), Britain's major credit union trade association, has taken the lead in trying to understand why many community credit unions attract only a few hundred members and how they can be supported to achieve greater growth. Among the factors that ABCUL has identified as restricting credit union growth rates in Britain are poor national legislation and inappropriate models of development.

It is commonly understood that current legislation in Britain is excessively restrictive and has been one of the main factors limiting the expansion of credit unions. An unpublished 1996 report from the World Council of Credit Unions stated, *"The current credit union legislation in Great Britain is amongst the most restrictive in the world"*. The Credit Union Act 1979 not only severely restricts the ability of credit unions to attract savings and to make loans but also limits the size, viability and scope of their common bonds. Over the last two years, ABCUL has been leading a campaign to modernise the legislation and the Government is now responding. Forthcoming changes in legislation will allow credit unions to offer a broader array of services and provide greater security for member savings, thereby significantly increasing the ability of credit unions to meet the needs of those who would most benefit from their services.

However, poor legislation alone does not explain why many credit unions have remained so small. For, despite the legislation, there are examples of both work-based and community credit unions that have grown significantly. A 1998 national research project[7], undertaken by Liverpool John Moores University in association with ABCUL, The Co-operative Bank plc and the English Community Enterprise Partnership, identified yet another factor that has held back the British credit union movement. The research found that many credit unions had been developed according to a particular organisational model which assumed that credit unions were very small (maybe only a few hundred members), entirely operationally organised by volunteers and aimed solely at very low income-base populations. In many ways, this model stressed the social objectives of credit unions to the exclusion of the economic objectives required for long term sustainable development. Instead of fostering the growth of a volunteer-led, professional co-operative financial service, able to meet the financial needs of large numbers of people, this model helped promote the image of credit unions as marginal poor people's banks. Undoubtedly this has restricted the growth of credit unions, even within the low income communities to whose needs the credit unions had aimed to respond.

Research conducted by Kempson and Whyley of the Personal Finance Research Centre identified *"that people on the margins of financial services want to deal with organisations which are financially secure, trustworthy and understand their needs"* [8]. Credit unions are, for the most part, successful in communicating trust and understanding the needs of their members. They grow out of existing social bonds either in work places, in organisations or within local communities. In fact, Fischer[9] has stressed the fundamental importance of pre-existing social bonds in the organisational development of credit unions. He has pointed to the fact that a credit union's success often depends on the strength of the social bonds on which the organisation is founded. However, it is clear that if they are to fulfil their potential, credit unions have to adopt models of organisational development that target long-term economic viability and ensure the financial security spoken about by Kempson and Whyley. As co-operative financial institutions, credit unions must operate to appropriate commercial standards and be able to offer a fully professional financial service to a large number of members. This involves using rigorous business development programmes to establish a wide and diverse membership base, to attract savers as well as borrowers and to ensure the quality of their service and financial products. In Britain, this will entail credit unions becoming less reliant on volunteers for the day-to-day operation of the organisation. The Liverpool John Moores University research revealed that 86% of community credit unions recognised that volunteer burn-out was restricting their growth. The increasing introduction of paid staff to run credit unions, whilst volunteers develop their role as policy makers and directors, seems intimately linked to long term security and quality of service. Significantly, Dalmuir Credit Union, in Scotland, with its 5,500 members, employs two full-time administrators and several part-time staff.

Credit unions necessarily compete in the financial market place. Hargreaves[10] writes *"the strong, clear message to co-operators is that there is no hiding place from the demands of competition. It is a case of compete or die. Organisations which provide goods or services which do not compete well in terms of price and quality will fail, whether they are owned by co-operators or tycoons chewing fat cigars"*. Where credit unions succeed, they are not regarded as old-fashioned nor decaying nineteenth century societies, but rather as modern financial institutions, particularly suited to responding the needs of middle and low-income groups. Wherever they are seen as a professional financial service, offering quality financial products, credit unions and credit co-operatives world wide are sustaining substantial growth. In Colombia, for example, between 1990 and 1994, the growth of assets in credit co-operatives exceeded the growth or assets in the investor-owned banks by a ratio of 3 to 1. At the end of 1993, credit unions had achieved penetration rates of 100% in Dominica, ranged from 30% to 49% in five other countries and from 10% to 29% in another 16 countries[11]. Growth rates in some countries, as in the United States and Ireland, have resulted in some strong reactions from the banks. In these countries, banks regard credit unions as increasingly strong competitors and have, perhaps somewhat inevitably, tried to instigate actions against credit unions in order to reduce their influence. In Britain, where credit unions are still, for the most part, in their infancy, the priority is to ensure that credit unions grow into economically secure financial institutions able to offer a quality, professional service to a much larger proportion of the population.

Important lessons from the US community development credit union movement

ABCUL has learnt some important lessons from the experience of the National Federation of Community Development Credit Unions (NFCDCU) based in New York. US community development credit unions serve predominantly low-income communities and tend, by US standards, to be smaller than mainstream credit unions. They have, on average, 1,300 members and around $2.4 million in assets per credit union. Yet, from the outset, these credit unions are established as professional financial institutions, most having secure premises and paid staff and with the capability of offering their members a range of financial services. They operate often with the support of a strong, credible sponsoring organisation and all have a business plan aimed at establishing economic viability within a short space of time. To this end, community development credit unions recruit 500-1,000 potential members, all of whom sign pledges of membership, before they ever open for business. Many of these credit unions are economically and socially very successful. Since 1980, for example, Self-Help, a community development credit union in Durham, North Carolina, has loaned $325 million (US) to low-income members - particularly Black people, women and rural residents - in order to buy homes, build businesses and strengthen community resources. Rosenthal and Levy, of the NFCDC, write that *"the best reason - and perhaps the only compelling reason - to organise a new credit union is to provide reasonably priced financial services to those who would otherwise not have access"* [12]. The Liverpool John Moores University research found that this clarity of focus was often lacking within smaller British community credit unions whose volunteers gave a range of reasons, often more social than economic, for organising credit unions. However, research findings confirm that more successful British work-based and community credit unions, like their US counterparts, have a much clearer vision of themselves as co-operative businesses aiming to offer a fully professional service within the financial services sector.

In order to assist credit unions to develop into financial institutions that are able to serve a large membership and to offer a wider range of services, ABCUL has drawn up a set of pre-requisites that any new credit union needs to have in place before it begins operation. At the same time, it has developed a series of national training seminars designed to ensure that any existing credit union, lacking these elements, is enabled to achieve them as soon as possible. Based on the experience of the US community development credit unions, ABCUL now considers that for any credit union to succeed, it must have all, or nearly all, the following elements in place:-

- a solid business plan, which targets growth and success.
- the effective leadership of a volunteer board and committees, consisting of individuals who are well regarded in the community and have the skills and vision to develop the credit union and make it grow.
- support and sponsorship from respected local institutions, to promote the credit union and give it credibility.
- initial funding or in-kind support to provide the credit union with:
  - ⇒ attractive premises, conveniently located to people in its community, and
  - ⇒ trained professional staff to operate the credit union
- an effective marketing and promotion programme capable of attracting at least 500 to 1000 members during the first few months of operation for new credit unions and at least 1000 to 2000 members for existing credit unions.

These elements, in one way or another, are found in successful credit union movements throughout the world. None of them compromise the basic commitment of credit unions to co-operative, mutual and social goals. However, wherever credit unions have grown significantly, they have all been established as professional financial institutions able to operate effectively within an increasingly competitive market place. This can be seen clearly within the Irish credit union movement as well as within the 365 credit and savings co-operatives that hold 32% of all domestic deposits in Cyprus. In Britain, the challenge is to consolidate progress so far and to ensure the sustainable development of the co-operative credit union financial sector.

Future support for the credit unions as unique financial organisations?

The British credit union movement is, in many ways, at a watershed. It can accept the Government's challenge to become a major provider of financial services, particularly for those on low incomes or facing financial exclusion. Or it can remain a movement, for the most part, marginal to the needs of mainstream British society. The Liverpool John Moores University research indicated that 76% of British credit unions are aiming to become, as their Irish and Cypriot cousins, a much more professional financial service. They already operate within established social bonds and networks. It is this that distinguishes them from banks and gives them a competitive edge within segments of the market inaccessible to, or avoided by, banks. They already have developed, in many cases, market niches through which those facing financial exclusion have access to low-cost financial services. What is needed currently is the investment, the support and organisational management expertise to ensure that all credit unions grow into the sustainable co-operative organisations that are found in other more mature credit union movements throughout the world.

Credit unions in Britain have currently two unusual, but powerful, sources of support; the municipal authorities and the banks. These are unusual in the sense that, in no other country in the world, have municipal authorities taken such a direct interest in the development of credit unions and, certainly, in most countries, credit unions are not so much supported by banks but regarded by them as serious competitors. In Britain, many municipal authorities see credit unions as key partners in the social and economic regeneration of communities. They regard the opportunities afforded by the co-operative ownership of credit unions as a real benefit in dealing with the particular problems of social and financial exclusion. Recently, the Local Government Association has drawn up new guidelines[13] for municipal authorities which aim, following ABCUL recommendations, to ensure that credit unions grow into large and economically viable organisations.

In a number of localities, credit unions have already developed profitable local relationships with banks. As Eileen Halligan, the administrator of Toxteth's Park Road Community Credit Union, points out. *"Park Road reaches the people that banks cannot or do not want to access. We're not in competition with them at all, we are in touch with the people they wouldn't touch at all"*. Park Road is, in fact, in negotiation with its local bank about opening the credit union in the bank premises on the two days when the bank itself will be closed. Clearly, banks have a responsibility to the communities from which they are withdrawing. There is a lot of suspicion in Britain that banks and building societies effectively black-list entire communities and make it incredibly difficult for anyone from those communities to access their services and facilities. A number of writers, for example Conaty and Mayo[14], consider that credit unions would benefit significantly if the Government were to introduce legislation similar to the US Community Reinvestment Act 1977 (CRA). This forces US banks and mainstream financial institutions to reinvest in the disadvantaged areas from where they take deposits. This re-investment has often been directed by banks through credit unions. However, in Britain, a more collaborative approach has been adopted. In the summer of 1998, the Government set a up a Treasury Task Force with the remit to explore ways in which banks and building societies could work more closely with credit unions to increase their effectiveness and widen their range of services. This Task Force consists of senior representatives from banks, building societies and the credit union movement and will publish its findings later in 1999. Indications are that its recommendation will be to establish a national central service organisation for all credit unions, equipped with the resources and personnel to provide the necessary organisational development support that credit unions in Britain currently need.

In Britain, as is proved throughout the world, credit unions have enormous potential to make an impact on the wider social economy and to deal with the social and financial exclusion of communities in ways banks never could, nor would, contemplate. In Britain, credit unions have a significant window of opportunity, insofar as both central and local government, together with the banks on the Government Task Force, are committed to supporting their growth and development as sustainable, modern financial organisations. That commitment of government, in the longer term, will need to be reflected at a European level. Credit unions in Britain and Ireland are currently exempt from European Banking Directives[15]. Any change in that exemption would serious hinder the development of the credit union movement. Even within the last year, the Irish Bankers Federation lodged two formal complaints with the European Commission claiming that the corporation tax exemption for credit unions amounted to unfair state aid and that credit unions should not be exempted from Banking Directives. Currently, the Irish credit unions are confident that, with Irish government support, this current challenge to the distinct and unique status of credit unions and credit-co-operatives will be rebutted. Yet, this is a serious issue for European credit union movement, including those movements in countries envisaging joining the European Community in the future. Credit unions are unique. As co-operative, democratic and mutual organisations, they make a real difference to the lives of ordinary people and, in particular, to excluded and marginalised groups in society. Credit unions grow out human and social values, but they only become really effective when, supported by appropriate legislation, regulation and taxation, they are enabled to grow large and strong enough to be able to deliver a range of low-cost financial services to people who need them the most.

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[1]*Figures taken from* Kempson E and Whyley C., Kept out or opted out? Understanding and combating financial exclusion. The Polity Press in association with the Joseph Rowntree Foundation. Biblios Publishers, West Sussex. 1999
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