FINANCIAL EXCLUSION IN THE SOUTH-EAST OF ENGLAND

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

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1. INTRODUCTION

The Small Change Partnership, consisting of Niamh Goggin of Small Change (N.I) Ltd, Paul Thain of Experian, Claire Caffrey and Charles Dodwell of the Community Development Finance Association and Peter Ramsden of Freiss, was commissioned by SEEDA to carry out two parallel research studies on financial exclusion in the South East of England.

The first commission, (Demand-Side Study) was to produce a baseline and mapping report into the extent and geography of Financial Exclusion in the South East. The report is to form the baseline evidence for the development of a regional Financial Inclusion Strategy in the region.

The second commission (Supply-Side Study) was to produce an in-depth assessment of the nature, extent and sustainability of Community Development Finance, including Credit Unions, in the Region and to make a realistic evaluation of whether, and to what extent, Community Development Finance Institutions and Credit Unions can deliver services to financially excluded individuals and communities on a sustainable basis.

The South-East of England is a powerhouse which, with London, drives the UK economy. In comparison with the rest of the UK, it has the highest economic activity rate, the lowest unemployment rate and the second-highest Gross Value Added (GVA) per head, at £18,400. The Thames Gateway Growth Area is the largest regeneration project of its type in Europe. The 2012 Olympic and Paralympic Games will act as a key driver for further economic transformation of the Region.

However, even such a successful regional economy cannot escape issues of social and financial inclusion. Almost 20% (900,000) of the workforce are economically inactive, of whom 250,000 report themselves as wanting to work. Black residents are 1.5 times and Asian residents are 2 times more likely to be economically inactive than white residents. There are also strong geographical contrasts within the region – GVA per head in the Thames Valley was 160% of the national average in 2002, compared to 61% in the Isle of Wight.

Poverty and disadvantage exist alongside a strong economic performance. Disadvantaged geographical communities and groups need the opportunity to build cohesive, sustainable communities. For many economically inactive and low paid South East residents, work and skills development are economically unviable. Increasing the economic viability of employment will require greater access to financial inclusion and advice services. In areas where the culture of worklessness is strongest, a holistic approach to workforce integration can link housing, education and skills, health, employment and financial services.

Some residents need also extra support in terms of a bridge to the mainstream employment market. Social enterprise and particularly intermediate labour market organisations can support reintegration and skills development of the most excluded. These organisations can also find themselves excluded from financial services as they do not fit standardised credit-scoring approaches.

Financial exclusion also costs the region economically. The Competition Commission Inquiry[1] on the supply of home credit in the UK found that the detriment to customers from an uncompetitive market may cost over £26 per loan amounting to £100 million per year. On a per capita basis, that would total over £13 million, which is being sucked out of the local economies where the poorest households in the South East of England are located. In addition, the cost of not having a bank account has been estimated by the New Policy Institute as 20-40% of average utility bills. At an average spend of £655.20[2], the seven per cent of households without a bank account in the South East[3] are losing a total of £4.62[4] million.

In terms of enterprise, the Global Entrepreneurship Monitor 2005 shows that the South East, previously second only to London in terms of the percentage of the adult population engaged in entrepreneurial activity, has seen its levels drop to equal those in the South West, at 7%, followed closely by the East of England at 6.5%. More significantly, the percentages trying to start a new business have dropped since 2003 from 6.8% to 5.3%, which will have an impact on future enterprise development.

Male entrepreneurship rates throughout the UK are significantly higher than those of females. In the South-East, the differential at almost 6% (4 % female vs. almost 10% male) is the highest in the UK. In fact, there has been a drop in female entrepreneurial activity between 2004 and 2005 from 4.5% to 3.9%. Women in rural areas are nearly twice as likely to be entrepreneurial as those living in urban areas (6.5% rural vs. 3.6% urban) and rural enterprise is a priority within SEEDA's Draft Regional Economy Strategy.

Although these statistics give a picture of personal and entrepreneurial financial exclusion and its impact in the South-East, they cannot provide the detail of the people who are financially excluded, who they are, where they are located and how many there are. In fact, no RDA has yet produced a detailed financial exclusion baseline and map. The Small Change Partnership, comprising Experian, Small Change (N.I.) Ltd and the CDFA, is pleased to present its pioneering methodology for measuring and mapping financial exclusion in the South-East of England.

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[1] The Competition Commission, Home Credit Market Inquiry, Summary of Provisional Findings, 2006.

[2] National Statistics, Family Expenditure Survey 2003

[3] Kempson, Prof E and Whyley, Claire, Understanding and combating 'financial exclusion', Findings, Joseph Rowntree Foundation, 1999

[4] 7% of 3,362,000 households in the South East, at an extra cost of £196.55 per household.

2. SCALE AND LOCATION[5] OF FINANCIAL EXCLUSION IN THE SOUTH-EAST

As part of the study, an Index of Financial Exclusion was constructed, which ranks Super Output Areas in the South East, using weightings produced by regression analysis against the Index of Multiple Deprivation. The median score is standardised at 100, giving a Financial Exclusion Index which ranges from 100 as the median score to 568.69 for the most financially excluded Super Output Area in the South East of England (E01016842 Milton Keynes).

The map overleaf shows the ranking of SOA's by level of financial exclusion. Extreme financial exclusion – 80-100% above the median is shown in dark red. Severe financial exclusion – 60 – 80% above the median is shown in red. High financial exclusion – 40-60% above the median - is shown in orange. Moderate financial exclusion – 20-40% above the median - is shown in dark yellow. Mild financial exclusion – 0 – 20% above the median – is shown in pale yellow. Areas which are not financially excluded are shown in white. Analysis in this report will focus on the SOA's suffering extreme financial exclusion – 80-100% above the median.

The local authority area with the highest number of SOA's in the worst 20% is Portsmouth, with 37 SOA's representing 55,500 people. It is followed by Southampton with 36 SOA's representing 54,000 people. The five local authorities with the highest number of SOA's are all in the Coastal South-East. They are Portsmouth, Southampton, Medway, Brighton and Hove and Thanet. The table below shows the full listing of LA's with SOA's in the worst 20% are:

Table 2: Ranking of Local Authorities by Scale of Financial Exclusion

Ranking	LA Name	# SOA's in worst 20%	Ranking	LA Name	# SOA's in worst 20%
1	**Portsmouth**	37	17	**Crawley**	5
2	**Southampton**	36	18	**Woking**	4
3	**Medway**	30	18	**Dartford**	4
4	**Brighton and Hove**	27	18	**Worthing**	4
5	**Thanet**	24	19	**Eastleigh**	3
6	**Milton Keynes**	20	19	**Adur**	3
7	**Slough**	19	19	**Fareham**	3
8	**Hastings**	17	19	**Cherwell**	3
9	**Gosport**	13	19	**Basingstoke & Deane**	3
9	**Dover**	13	20	**Rushmoor**	2
9	**Swale**	13	20	**New Forest**	2
10	**Havant**	12	20	**Reigate Banstead**	2
11	**Shepway**	11	20	**Tunbridge Wells**	2
12	**Canterbury**	10	20	**Aylesbury**	2
12	**Gravesham**	10	20	**Guildford**	2
12	**Oxford**	10	21	**Winchester**	1
12	**Eastbourne**	10	21	**Mole Valley**	1
13	**Reading**	9	21	**Lewes**	1
14	**Arun**	8	21	**Test Valley**	1

[5] Methodology detailed in Chapter 4, Financial Exclusion Baseline and Mapping, Small Change Research Partnership, SEEDA, 2006

15	**Maidstone**	7
15	**Isle of Wight**	7
16	**Rother**	6
16	**Wycombe**	6
17	**Ashford**	5
21	**Bracknell Forest**	1
21	**Wealden**	1
21	**South Oxfordshire**	1

Personal Financial Exclusion at Super Output Area

Ranking of SOA by Level of Financial Exclusion

- Extreme financial exclusion - 80 - 100% above the median
- Severe financial exclusion - 60 - 80% above the median
- High financial exclusion - 40 - 60% above the median
- Moderate financial exclusion - 20 - 40% above the median
- Mild financial exclusion - 0 - 20% above the median
- Not financially excluded

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The table showing the number of Super Output Areas in the worst 20% by Local Authority demonstrates the scale of financial exclusion. As SOA's have a mean population of 1,500 people, the 411 SOA's represent 616,500 people in the South-East whose access to financial services is extremely restricted. Many of these people are located in large local authority areas with high concentrations of financial exclusion. However, it is notable that many local authorities which rank low on the Index of Multiple Deprivation have a small number of SOA's which are extremely financially excluded. These include Rushmoor, New Forest, Reigate and Banstead, Tunbridge Wells, Guildford, Winchester, Mole Valley, Test Valley, Wealden and South Oxfordshire. The relatively small numbers of financially excluded people concerned and their concentration in limited geographical areas should make it possible to target resources and activities to solve this issue.

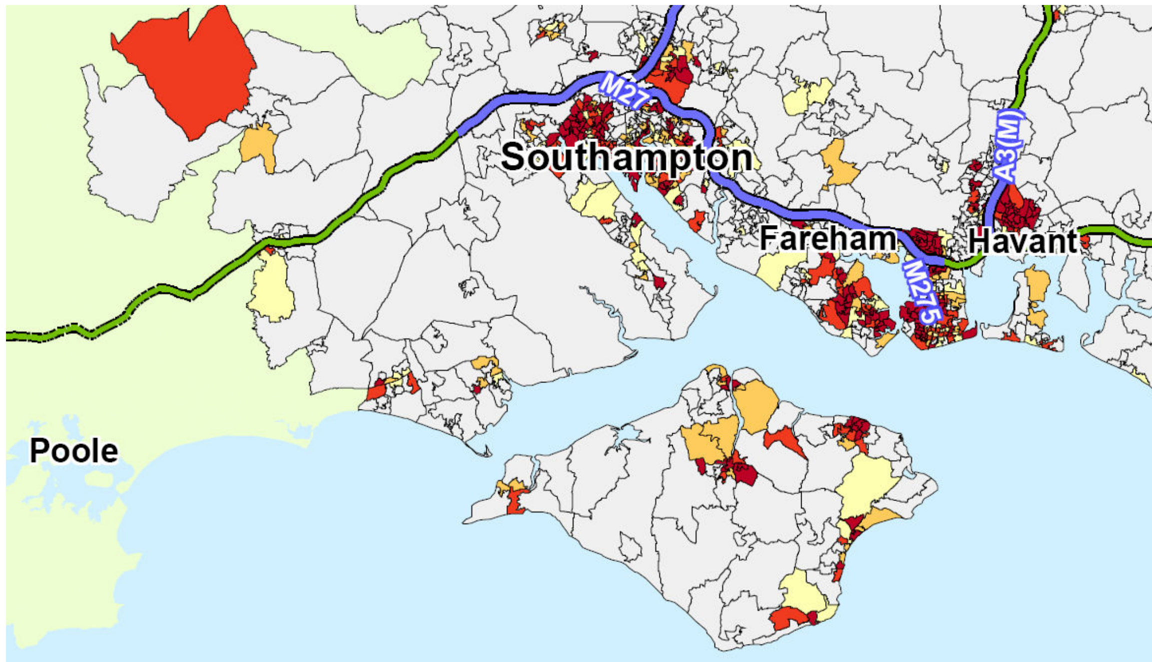
Financial exclusion is an issue, not just of scale but also of intensity. A concentration on numbers does not reflect the depth of financial exclusion in smaller local authority areas. The table below ranks local authorities by the percentage of SOA's in the worst 20%:

Table 3: Ranking of Local Authorities by Intensity of Financial Exclusion

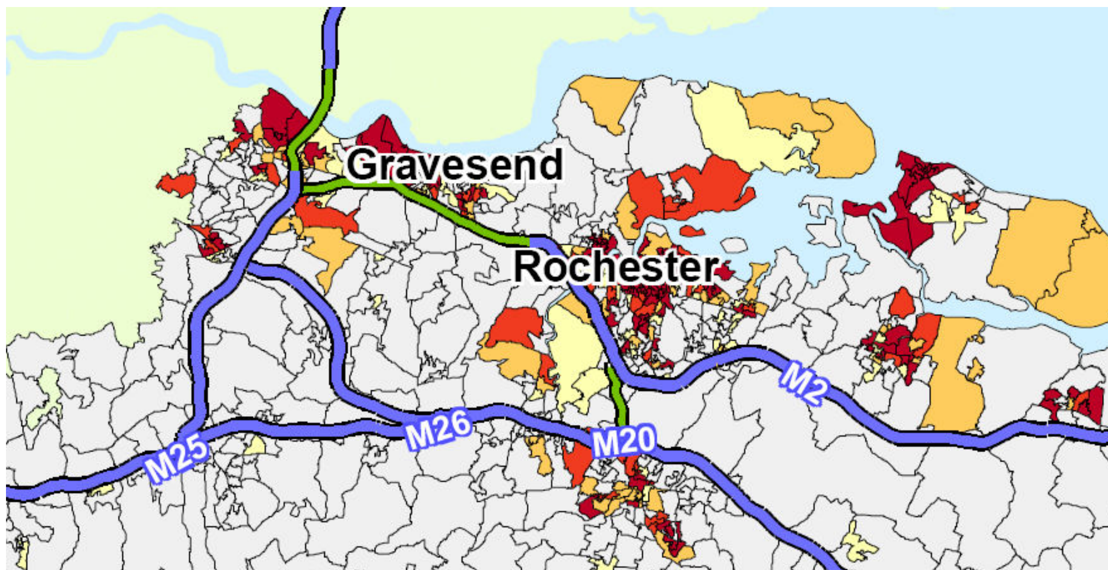
Ranking	LA Name	%SOA's in worst 20%	Ranking	LA Name	% SOA's in worst 20%
1	**Portsmouth**	5.87%	25	**Adur**	1.46%
2	**Hastings**	5.59%	26	**Dartford**	1.41%
3	**Thanet**	5.38%	27	**Woking**	1.33%
4	**Slough**	5.26%	28	**Wycombe**	1.16%
5	**Gosport**	5.16%	29	**Worthing**	1.13%
6	**Southampton**	4.93%	30	**Fareham**	0.85%
7	**Medway**	3.74%	31	**Eastleigh**	0.79%
8	**Dover**	3.67%	32	**Rushmoor**	0.71%
9	**Shepway**	3.27%	33	**Cherwell**	0.70%
10	**Gravesham**	3.26%	34	**Basingstoke and Deane**	0.59%
11	**Swale**	3.25%	35	**Tunbridge Wells**	0.57%
12	**Havant**	3.11%	36	**Reigate and Banstead**	0.48%
13	**Eastbourne**	3.05%	37	**Guildford**	0.47%
14	**Milton Keynes**	2.96%	38	**Aylesbury**	0.38%
15	**Brighton and Hove**	2.94%	39	**Mole Valley**	0.36%
16	**Oxford**	2.42%	40	**New Forest**	0.34%
17	**Canterbury**	2.22%	41	**Lewes**	0.31%
18	**Reading**	1.94%	42	**Bracknell Forest**	0.29%
19	**Rother**	1.92%	43	**Winchester**	0.28%
20	**Arun**	1.57%	44	**Test Valley**	0.28%
21	**Crawley**	1.55%	45	**South Oxfordshire**	0.23%
22	**Isle of Wight**	1.54%	46	**Wealden**	0.21%
23	**Maidstone**	1.52%			
24	**Ashford**	1.46%			

The construction of a Financial Exclusion Index has allowed for the first time the identification of location, scale and intensity of financial exclusion in the South-East. The 411 SOA's which are characterised by extreme financial exclusion (80-100% above the mean) represent approximately 616,500 people. These areas are shown in the maps below in dark red, with severe financial exclusion being shown in lighter red, high financial exclusion in orange, moderate in dark yellow and mild financial exclusion in pale yellow. Areas which are not financially excluded are shown in white. The five local authorities with the highest number of SOA's in the worst 20% are all in the Coastal South-East (Portsmouth, Southampton, Medway, Brighton and Hove and Thanet) and we estimate that 231,000 people in those five areas suffer from extreme financial exclusion.

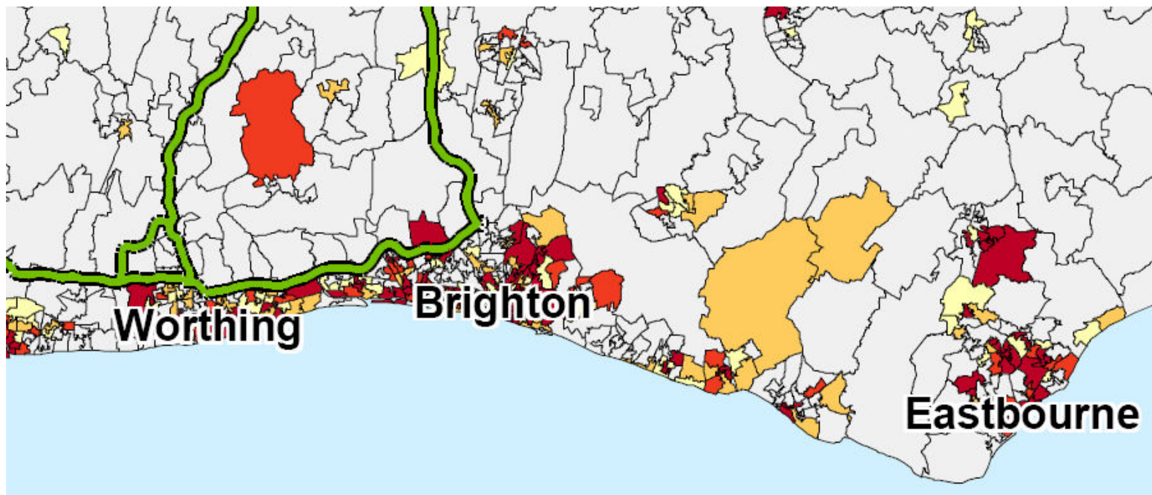
Financial Exclusion in the Southampton and Portsmouth Areas:



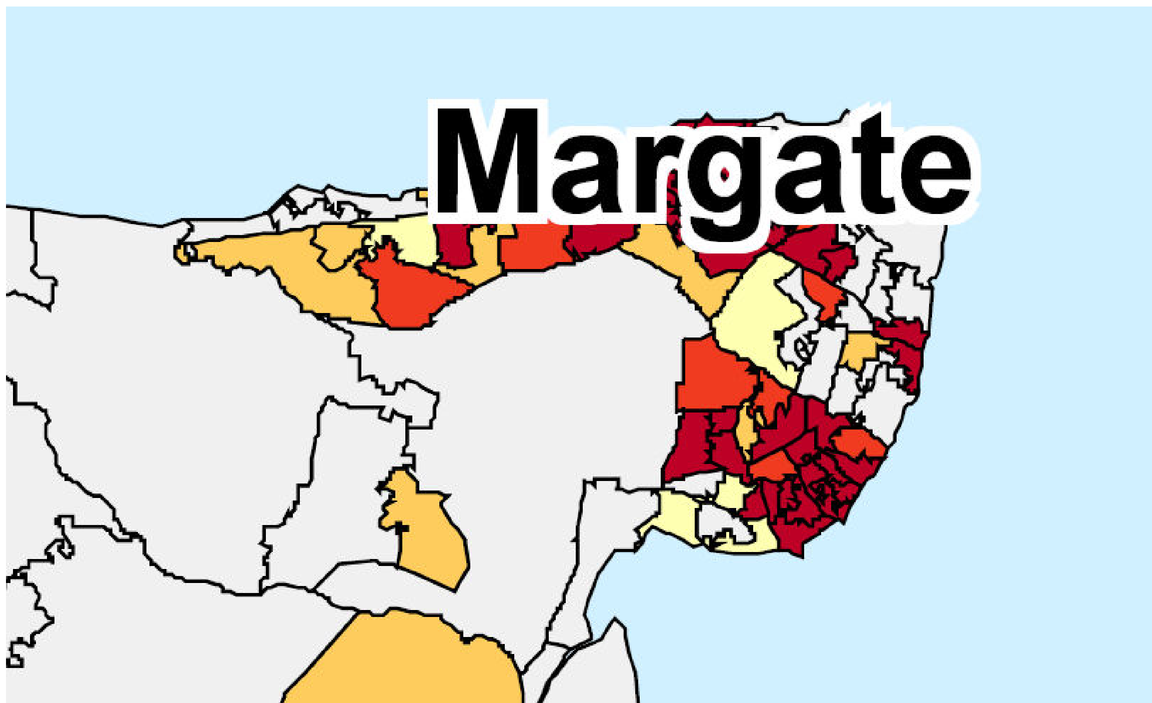
Financial Exclusion in Medway:



Financial Exclusion in Brighton and Hove



Financial Exclusion in Thanet:



As well as focusing on scale, the report shows that intensity of financial exclusion is particularly severe in some of the smaller local authorities such as Hastings, Thanet, Slough and Gosport. Finally, many local authorities which rank low on the Index of Multiple Deprivation have small pockets of extreme financial exclusion. The relatively small numbers of financially excluded people concerned and their concentration in limited geographical areas should make it possible to target resources and activities to solve this issue.

3. PERSONAL FINANCIAL EXCLUSION: HOW MANY AND WHO ARE THEY?

NO SAVINGS ACCOUNT: 278,032 HOUSEHOLDS

We estimate that 278,032 households, comprising 8.8% of households in the South-East region do not have access to a savings account. The term "access to" is used to indicate that we do not know whether individuals in the household have ever applied for a savings account and been refused, whether they lack the confidence to apply for an account or whether they never wanted a savings account. The same phrase is used in relation to other financial services.

The types of households who do not have access to a savings account include:

- Single parents, predominantly female in their twenties or early thirties, renting local authority or housing association properties, usually terrace houses or flats for whom debt is often a problem.

- Older families living in local authority or housing association terraced housing, with extended families including a dependent parent. They are approaching retirement, often manual workers. They are at high risk of unemployment. They have small levels of debt. Their pensions are inadequate. Their most likely ethnicity is Scottish or Irish, although they also include people originating from North Africa, the Middle East, Bangladesh and Pakistan. They have low take-up of telephones.

- Poorest pensioners, single and living alone, high number of females, living on basic pension in Council flats with unsustainable debt levels. They have no phone or mobile phone and don't use the Internet. Fewer ethnic minorities.

- Homesharers

- Range of ethnicities – European, African, Middle Eastern, Bangladeshi, Pakistani, Indian or East Asian;

- Housewives;

- People who are unemployed or work part-time.

NO CURRENT ACCOUNT: 146,380 HOUSEHOLDS

It is estimated that 146,380 households, comprising 4.6% of households in the region, do not have access to a current account. They share many characteristics of those who do not have access to a savings account, but they do not include the older families where access to a bank account is probably dictated by work or benefit claims.

NO AFFORDABLE PERSONAL CREDIT: 207,159 HOUSEHOLDS

An estimated 207,159 of households in the region (6.6%) do not have access to affordable credit. Their characteristics are quite different from those of the previous two categories. They include:

- Young singles – 20's to early 30's

- Female homesharers

- Young single parents, predominantly female
- Households with no full-time earner / unemployed.

They live in local authority or housing association housing and are likely to be of North African, Middle Eastern, Bangladeshi or Pakistani origin. They purchase from mail order catalogues, are likely to have mobile phones and to receive information by SMS text messaging.

Another group in this category is made up of single thirty-somethings, both male and female with young children. They are homesharers who live in local authority housing. They live within their means and are not in debt. They are familiar with new technology and the internet. Their ethnic background may include European, African, Middle Eastern, Bangladeshi, Pakistan, Indian or East Asian. They have mobile phones and receive information by SMS text messaging.

NO HOME CONTENTS INSURANCE: 310,850 HOUSEHOLDS

310,850 households in the South East (9.9% of households) do not have access to home contents insurance. Three main demographic groups were represented in this category:

- Young singles and student households sharing homes in private flats and terraced houses. They have poor finances including student loans. Many are of East Asian, North African, Middle Eastern, Bangladeshi or Pakistani origin. Their Internet usage is high and they use mobile phones rather than landlines. They juggle their debt on credit cards;
- Young single parents living alone with young children. They have basic bank accounts. They have low incomes, insecure jobs and problems with debt. If they own their own homes, property values are low. They use mobile phones;
- Retired singles with some savings and no mortgages living in bungalows. They have low income and expenditure. They do not use phones, mobiles or the Internet.

NO ACCESS TO CREDIT CARDS: 142,407 HOUSEHOLDS

Two main groups make up those 142,407 households (4.5% of households in the region) who do not have access to credit cards. They are:

- Poorest pensioners, mainly female and single who live alone. They live on the basic pension in Council flats. They have unsustainable levels of debt. They have no phones or mobile phones and don't use the Internet. They include fewer ethnic minorities;
- Single parents, predominantly in their 20's or early 30's living in local authority or housing association properties. Debt is a problem for them.

Other characteristics in this category include homesharers, ethnic minorities, housewives, the unemployed and those working part-time, often with low or negative net worth. Their Internet usage is low.

NO ACCESS TO MONEY ADVICE: 73,600 HOUSEHOLDS

Most debt problems relate to credit debts, rather than mortgage arrears or community charge arrears. Women, tenants of social landlords and the unwaged were most likely to have debts associated with poverty, such as catalogue debts and loans to doorstep lenders. The main reasons why CAB clients got into debt included job loss, ill-health and relationship breakdown, over-commitment and poor

money management. FSA research has suggested that 1.5 million people in the UK are falling behind with bills or credit commitments. On a pro-rate basis, this would apply to 200,000 people or 80,000 households in the South-East and would indicate that CAB's, even with a significant increase in the number of cases they are handling, are now reaching 8% of the potential demand for debt advice.

SUMMARY

Table 7: Scale of Financial Exclusion by Product / Service

	Number of households	**% of households in SE Region**
No access to savings account	278,032	8.8%
No access to current account	146,380	4.6%
No access to affordable personal credit	207,159	6.6%
No access to contents insurance	310,850	9.9%
No access to credit cards	142,407	4.5%
In need of debt advice	73,600	2.3%
South East Region	**3,154,846**	**100%**

The statistics show that between 4.5 and 9.9% of households in the South-East of England are excluded from basic financial services. A basic bank account is now seen as a prerequisite for participation in a modern economy, yet over 145,000 households don't have one. Most of the households above are probably living in social housing which could provide contents insurance as a basic risk-mitigation tactic, yet over 310,000 households don't have access to it. 80,000 households are estimated as being in need of debt advice of whom over 8% were received it in 2004/05. Given the relatively small proportion of households involved and the prosperity of the South-East Region, this is a challenge which can be overcome through properly targeted intervention.

4. ENTERPRISE FINANCIAL EXCLUSION

It is estimated that there are 252,450 registered and 343,339 unregistered businesses in the region, with 71,923 registered and unregistered start-ups every year. Of these, 77,336 businesses (12.98% of the total) seek and are refused finance every year. It is estimated that 9,381 or just over 12% are CDFI-viable, that is they would be willing to approach a CDFI for finance, that their proposition itself is viable and that the CDFI would be able to lend to them. Of those businesses, 3,596 would be start-ups, 5,493 would be existing micro-enterprises (<10 employees) and 292 would be small businesses (10 – 50 employees).

Table 8: Estimated Enterprise Financial Exclusion in South-East

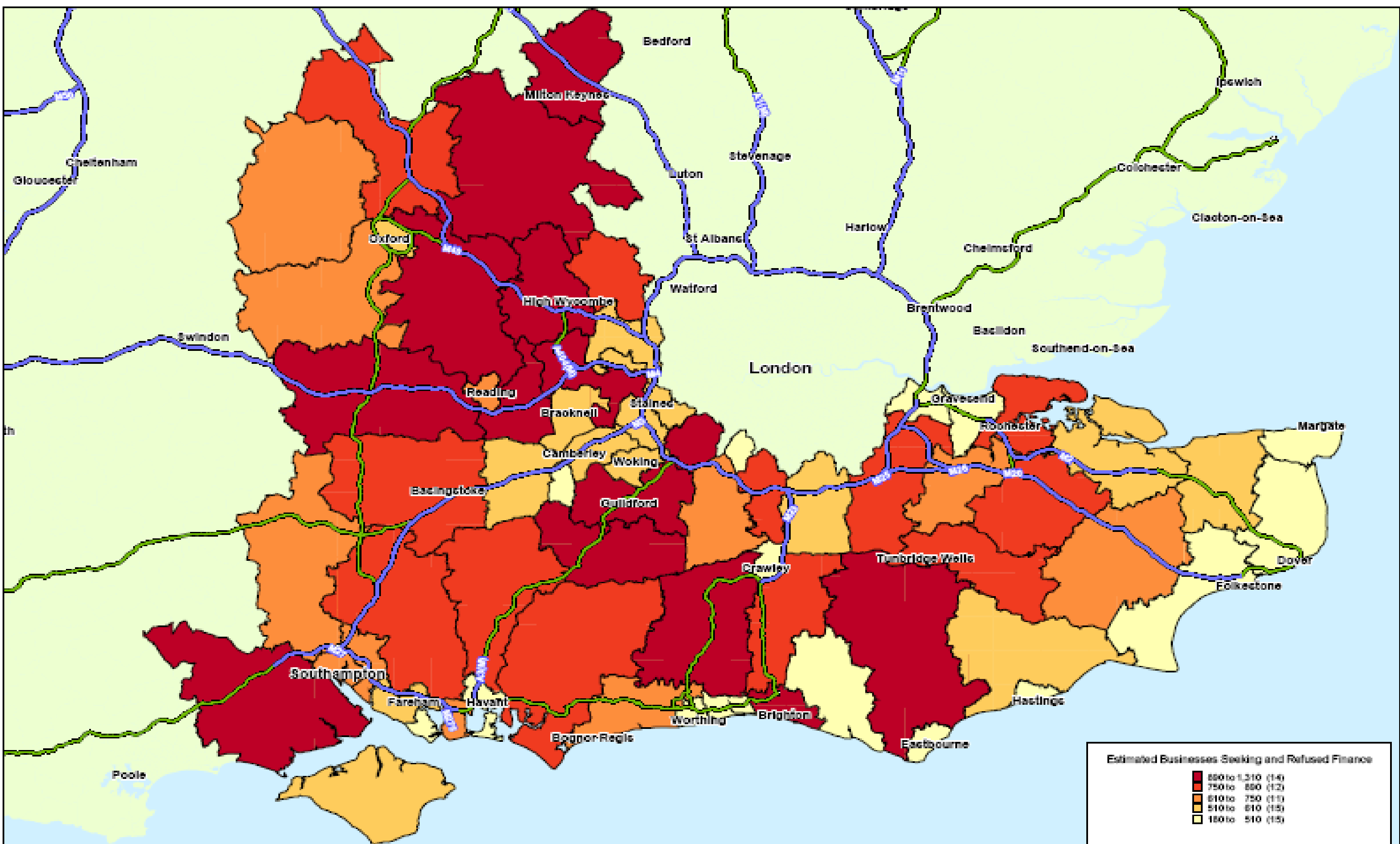
Estimated total businesses	Estimated businesses seeking and refused finance	% Refused Finance	Start-up CDFI-viable	Micro CDFI-viable	SB CDFI-Viable	Total CDFI-viable
595899	**77336**	**12.98%**	**3596**	**5493**	**292**	**9381**

Looking at enterprise financial exclusion on a local authority basis, the authority with the highest numbers of excluded businesses is Brighton and Hove, followed by Wycombe, Milton Keynes and Aylesbury Vale. The table below shows the fourteen LA's with the highest numbers of excluded businesses. The full extent of enterprise financial exclusion illustrated by the map overleaf:

Table 9: 20 LA's with Highest No's of Excluded Businesses

LA Name	Estimated total businesses	Est. businesses refused £	% Refused Finance	Start-up CDFI-viable	Micro CDFI-viable	SB CDFI-Viable	Total CDFI-viable
Brighton and Hove	16866	2403	14.25%	127	151	7	286
Wycombe	16370	2044	12.49%	89	152	9	250
Milton Keynes	14847	2016	13.58%	100	133	9	242
Aylesbury Vale	15048	1893	12.58%	84	142	5	232
Windsor /Maidenhead	14599	1903	13.03%	89	135	7	231
West Berkshire	14399	1819	12.64%	81	133	8	222
Wealden	13832	1689	12.21%	71	132	5	208
South Oxfordshire	13278	1657	12.48%	73	125	6	203
Elmbridge	12487	1650	13.21%	79	115	5	200
New Forest	12924	1627	12.59%	72	120	6	199
Waverley	12487	1630	13.06%	77	115	6	198
Wokingham	12086	1608	13.31%	78	111	5	194
Medway	11307	1524	13.48%	75	103	6	183
Guildford	11613	1502	12.94%	70	108	5	183

Enterprise Financial Exclusion by Local Authority



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However, looking at enterprise financial exclusion purely in terms of the potential size of the market risks losing focus on the emphasis on enterprise in deprived communities as a tool for social inclusion. The following table ranks the enterprise exclusion demand according to the Index of Financial Exclusion developed for personal financial services:

Table 10: Enterprise Financial Exclusion in the Most Excluded LA's

Ranking	LA Name	Start-up CDFI-viable	Micro CDFI-viable	SB CDFI-Viable
1	Portsmouth	54	73	5
2	Hastings	25	36	2
3	Thanet	38	46	3
4	Slough	48	57	6
5	Gosport	14	23	1
6	Southampton	64	85	6
7	Medway	75	103	6
8	Dover	32	48	3
9	Shepway	32	52	2
10	Gravesham	31	44	2
11	Swale	46	68	4
12	Havant	33	56	3
13	Eastbourne	34	39	2
14	Milton Keynes	100	133	9
15	Brighton and Hove	127	151	7
16	Oxford	40	61	5
17	Canterbury	44	69	4
18	Reading	51	81	6
19	Rother	34	64	2
20	Arun	53	80	4
21	Crawley	32	40	3
22	Isle of Wight	42	69	4
23	Maidstone	71	101	6
24	Ashford	54	79	4
25	Adur	18	30	2

SOCIAL ENTERPRISE FINANCIAL EXCLUSION

Many social enterprises do not understand commercial bank finance, don't know what it requires or how to get it and the "Lending to the Social Economy" Report[6] viewed this as a major barrier to their future growth and success.

Financially excluded social enterprises are likely to be:

- Smaller than those already availing of bank funding;
- Lacking physical collateral;

[6] Shorebank 2004

- Highly risk-averse
- Afraid of being rejected if they apply
- Receiving less than 25% of their income from trading;
- Lack financial management capacity;
- Lacking information about sources of finance;
- Interested in diversifying their income

Social enterprises are widely distributed throughout the region, although less likely[7] to be located in the top 20% or the 20-40% most deprived regions than elsewhere in the UK. 86% are urban and 14% rural, against an 89%/11% split in the UK as a whole. Their turnover and size profiles match those in the rest of the UK. They are more likely to work with people and less likely to work with the environment. They are significantly less likely to be involved in real estate / property rental or business education. They have fewer full-time and more part-time employees than average.

[7] IFF Research, 2005

5. PERSONAL FINANCIAL SERVICES IN THE SOUTH-EAST

Personal finance service providers include credit unions which offer savings accounts, loans, children's savings accounts as well as budgeting and debt advice. Leading Credit Unions in the Region are also introducing new accounts similar to bank current accounts with cashcards as well as cash ISA's. Our surveys identified twenty credit unions working in the Region, of whom responses were received from fourteen. The other main personal finance provider in the South-East is South Coast Money Line (formerly Portsmouth Area Regeneration Trust), which is a CDFI and provides personal and micro-enterprise loans as well as advice and support.

The survey shows that of the 2,346 personal loans made in the South-East last year, over 2,000 of them were made by the top six providers. The ranking of providers in terms of number of loans is:

Table 2: Ranking of Personal Finance Providers by Scale

Ranking	Provider Name:	No. Loans
1	Portsmouth Savers Credit Union Ltd	863
2	South Coast Money Line	361
3	City of Brighton & Hove	268
4	Isle of Wight Credit Union Ltd	250
5	Crawley Credit Union Limited	145
6	Isle of Thanet Credit Union Ltd	144
7	Hastings and St Leonards Credit Union Ltd	84
8	Medway Credit Union Limited	80
9	Central Sussex Credit Union	40
10	Southampton Co-operators Credit Union Ltd	38
11	Eastleigh Credit Union Limited	25
12	District of Canterbury Credit Union Limited	25
13	Family Assurance .. Employees CU	12
14	Oxford & District Credit Union Ltd	11
	TOTALS:	2,346

The local authority areas which suffer from substantial levels of financial exclusion but have no service are:

- Slough
- Dover
- Shepway
- Gravesham
- Swale
- Arun
- Maidstone
- Ashford
- Adur.

In addition, there are a number of areas where a credit union or other provider is in existence, but is not managing to reach its target group by achieving more than 50 loans per year. These areas include Eastbourne, Milton Keynes, Oxford, Canterbury and Reading. Finally, in terms of coverage, the dispersed spatial characteristics of deprivation in the South East – an archipelago of poverty means that concentrations of poverty and social exclusion can be found in almost every district. Although these may not feature in the 20% most financially excluded, SOA's in some of the most prosperous areas such as E01004108 Sutton at No. 629 in the Financial Exclusion Index and E01002919 Kingston upon Thames at No. 726 are 60-80% above the median and are characterised in the Financial Inclusion Demand Report as severely financially excluded.

6. ENTERPRISE FINANCIAL SERVICES

MICROFINANCE

Microfinance is the provision of small-scale enterprise finance to the self-employed or very small businesses. The EU defines microfinance as referring to average loan sizes under €25,000 (approximately £16,000) and in the UK it refers to loans to enterprises with fewer than 10 employees, most frequently to the self-employed, sole traders and businesses with fewer than five employees.

Our study identified seven microfinance providers operating in the South East, of whom two are national organisations and four are sub-regional. In addition to access to finance, they provide a range of advice, support and sign-posting to other business services. The organisations are listed in the table overleaf in order of the number of loans provided in the last financial period.

The Prince's Trust provides finance and support for under 30's on a national level and is providing the largest number of loans in the Region at 241. It is followed by Fredericks Foundation with 145 loans, which focuses its support on five groups of people: Financially Disadvantaged, Unemployed, Single Parents, Ex-Offenders and the Disabled. South Coast Money Line, covering Portsmouth, Havant, Gosport and Southampton which is the only CDFI operating in the region to provide personal and enterprise finance, made 64 enterprise loans in the past year, reaching the most financially excluded clients. Capitalise is a relatively new CDFI, just two years old, but has established itself well in Sussex and part of Kent. Enterprise Loan Fund has made 36 loans in Dartford, Gravesham, Medway and Swale.

Table 4: Ranking of Microfinance Providers by Scale

	Microfinance Provider	No. Loans PA
1	The Prince's Trust	241
2	Fredericks Foundation	145
3	South Coast Money Line	64
4	Capitalise Business Support	45
5	Enterprise Loan Fund	36
6	Isle of Wight Lottery	6
7	Prime	1
	TOTALS	518

Prince's Trust covers the whole region and therefore ensures that young people under the age of 30 receive good advice and support services as well as access to finance. Prime was established to provide a similar service for people over the age of fifty, but has not yet made an impact in terms of delivery (1 loan last year).

Financially excluded areas which have no enterprise coverage for over 30's include:

- Dover
- Milton Keynes
- Oxford.

Other, better-off areas without coverage include Buckinghamshire, South Kent, parts of Hampshire and Oxfordshire. There is a serious market gap in the North of the Region affecting Milton Keynes in particular and also Oxford. It seems likely that with the expansion of Milton Keynes/South Northamptonshire, the market potential for a CDFI in the area will grow. Given the serious levels of deprivation in Corby the potential for a CDFI crossing regional boundaries should not be ruled out. These areas are illustrated by the Enterprise Financial Exclusion Map on the previous page.

Within the enterprise lending sector, Prince's Trust is a dynamic national player with the potential for steady growth in its loan portfolio. At sub-regional level, South Coast Money Line, Fredericks Foundation and Capitalise all look capable of growing significantly if appropriate funding arrangements can be organised at regional level. Enterprise Loan Fund is not currently employing lending staff but has the infrastructure to provide coverage in the Greater Medway area.

There is likely to be some overlap as some of the larger players grow into adjacent territories and some competition between the regional and national players. Our suggestion is that in the first instance, the sub-regional players should attempt to enlarge the spatial coverage on their core markets without entering into direct competition with the other CDFI's. This would appear to be justified because all of the sub-regional organisations are dependent on public funding. Because of the specific market specialisms that are being developed – for example South Coast Money Line's home improvement loans and Fredericks Foundation's work with micro-entrepreneurs who have suffered mental illness – it is possible that in some product areas, there will be considerable spatial overlap but without having direct competition between products.

Where there are overlaps in coverage, it is likely that CDFI's can offer a form of stepped offer where one lender makes the first and perhaps riskiest loan and then graduates the lending to other, larger CDFI lenders and finally to the banks.

MICRO / SMALL BUSINESS LENDING

The average enterprise loan size from the six lenders is £3,555 and ranges from £7,500 (Capitalise) down to £910 (South Coast Money Line). South East Community Loan Fund offers loans ranging from £15,000 to £50,000 to incorporated SME's in the 20% most deprived wards in the Region. The average loan size is expected to be £25,000. CDFI SME lending in the UK amounts to 9.4% of portfolio value at almost £5 million, although this is concentrated in a small number of regions.

This implies that there is a small market gap in the South East for borderline micro/ SME lending including to businesses in deprived areas. There is an opportunity for the six sub-regional lenders to co-operate in providing a regional small business loan product in the range £7,500 to £20,000, averaging £15,000. This will increase investment in deprived communities while strengthening CDFI sustainability.

The table overleaf shows the estimated demand for this type of lending by local authority area:

Table 8: Estimated Micro / Small Business Lending Demand

LA code	LA name	Estimated Micro / Small Business Lending Demand
00ML	Brighton and Hove	7
11UF	Wycombe	9
00MG	Milton Keynes	9
11UB	Aylesbury Vale	5
00ME	Windsor and Maidenhead	7
00MB	West Berkshire	8
21UH	Wealden	5
38UD	South Oxfordshire	6
43UB	Elmbridge	5
24UJ	New Forest	6
43UL	Waverley	6
00MF	Wokingham	5
00LC	Medway	6
43UD	Guildford	5
29UH	Maidstone	6
45UF	Horsham	5
45UG	Mid Sussex	5
24UB	Basingstoke and Deane	6
38UB	Cherwell	6
29UK	Sevenoaks	5
24UC	East Hampshire	5
43UF	Reigate and Banstead	4
45UD	Chichester	5
11UC	Chiltern	3
24UP	Winchester	5
00MS	Southampton	6
29UQ	Tunbridge Wells	4
38UF	West Oxfordshire	5
38UE	Vale of White Horse	4
24UN	Test Valley	5
45UC	Arun	4
00MC	Reading	6
29UB	Ashford	4
24UD	Eastleigh	6
00MR	Portsmouth	5
43UE	Mole Valley	3
29UP	Tonbridge and Malling	5
11UE	South Bucks	3
24UG	Hart	3
43UK	Tandridge	3
29UM	Swale	4
43UJ	Surrey Heath	3
00MA	Bracknell Forest	4
29UC	Canterbury	4
00MW	Isle of Wight	4
43UM	Woking	4

LA code	LA name	Estimated Micro / Small Business Lending Demand
00MD	Slough	6
24UE	Fareham	4
38UC	Oxford	5
43UH	Spelthorne	3
43UG	Runnymede	3
21UG	Rother	2
21UF	Lewes	3
24UH	Havant	3
29UN	Thanet	3
29UL	Shepway	2
45UH	Worthing	3
29UD	Dartford	3
29UE	Dover	3
24UL	Rushmoor	3
29UG	Gravesham	2
43UC	Epsom and Ewell	2
45UE	Crawley	3
21UC	Eastbourne	2
21UD	Hastings	2
45UB	Adur	2
24UF	Gosport	1
	Totals	292

SOCIAL ENTERPRISE FINANCE

The main social enterprise CDFI's in the South-East are:

- Co-operative and Community Finance (formerly ICOF)
- Charity Bank
- Local Investment Fund / South East Community Loan Fund
- BIGInvest
- Triodos Bank.

As these are national organisations, only LIF/SE Community Loan Fund has provided a regional breakdown of its loans. LIF has made 6 loans in 2005/06 totalling £400,000. However, from discussions with most of the other providers and the opportunity to review their national lending figures, our estimate is that roughly 21 CDFI social enterprise loans were made in the South-East in the last financial year. This is less than one-third of what might be expected in the South-East on a pro-rata basis and a tenth of the estimated total demand in the Region.

It is clear that there is neither a shortage of social enterprise finance providers nor of capital for lending. The particularly low performance in the South-East seems due to a combination of reasons. These include the perception among the sector that the Region is relatively prosperous and therefore not a priority area. Also, social enterprises in the South-East are significantly less likely to be involved in real estate or property rental, sectors which often drive borrowing. They also have fewer full-time employees and are therefore likely to have less management resource to develop new enterprises or projects that require funding.

There does not appear to be any gap in market for social finance in the South-East that cannot be filled by current providers.

WHOLESALE PROVISION

All five of the large social enterprise lenders, BIGInvest, Charity Bank, ICOF, LIF and Triodos, are accredited by the Small Business Service to use Community Investment Tax Relief and can wholesale funds for onlending to other CDFI's. Both Charity Bank, on behalf of the Esmee Fairbairn Foundation, and Co-operative and Community Finance have provided wholesale funds to Portsmouth Savers Credit Union to increase their available loan capital. Wholesaling money in this way brings a private sector discipline to CDFI's and forces the development and transparency of financial and social reporting systems. While smaller CDFI's may require some capital grants in particular where they are extending their operations into new areas or products, it is important that neither grants nor soft loans damage this developing capital market for CDFI's.

7. GAPS ANALYSIS

COVERAGE GAPS

In terms of scale, the major coverage gap in financial inclusion services is in the area of personal finance. At present, 12% of the potential demand of over 20,000 fair finance loans is being supplied by existing providers. Of the 2,500 loans being provided, 85% come from the six largest organisations, five credit unions and one CDFI. These organisations need to scale up their operations substantially to meet the unmet demands for service, as Portsmouth Savers, South Coast Money Line and Brighton and Hove have shown that they can do.

In terms of micro-enterprise lending, an estimated 5.7% of the 9,089 loan demand is currently being met. The six enterprise lenders need to increase their scale of operation significantly, both to meet demand and to move towards sustainability.

The main coverage gap in the provision of enterprise financial inclusion services is in the gap between micro and small business lending. There is a gap in the market for loans between £7,500, which existing CDFI's are providing and £20,000 plus, which are provided by the South East Community Loan Fund, in disadvantaged areas. While the market is not huge, it would best be served by a joint approach by all six enterprise CDFI's offering a standard loan product to businesses across the region. This would require both access to loan capital and the development of standard loan application and analysis processes.

At the outset, it is obvious that there is no gap in the provision of social enterprise finance in the Region, but that work is needed to develop confidence and skills in a relatively weak market. Rather than increasing grant aid directly to social enterprises or indirectly through finance providers, investment could be made in education and business support for the sector so that it becomes more ambitious and professional in its social enterprise operations.

GEOGRAPHICAL GAPS

In terms of personal financial exclusion services, there are significant geographical gaps in some of the most financially excluded and deprived areas in the South-East. These are:

- Berkshire: Slough
- Kent: Ashford, Dover, Shepway, Gravesham, Maidstone, Swale
- West Sussex: Arun Adur

In Eastbourne, Milton Keynes, Oxford, Canterbury and Reading, the credit unions in existence have not yet managed to make a significant impact in terms of numbers of members or loans. Finally, there are small pockets of extreme financial exclusion in almost every district. The relatively small numbers of people involved and their geographical concentration means that this is a problem which can be solved by a concentrated and focused partnership by local authorities, housing associations, banks and building societies, credit unions and CDFI's, co-ordinated in a Regional Financial Inclusion Framework by SEEDA.

For microfinance concentrating on financially excluded areas, there are gaps in provision in Dover, Milton Keynes and Oxford. There are also significant underserved markets in the more prosperous areas such as Wycombe, Aylesbury Vale, Windsor and Maidenhead, West Berkshire, Wealden, South Oxfordshire, Elmbridge, New Forest, Waverly, Wokingham and Guildford.

There is no geographical gap in social enterprise lending or wholesale lending to CDFI's or Credit Unions for onlending. Some investment readiness work is likely to be needed with the region's social enterprises to prepare them for loan finance.

PRODUCT GAPS

Leading credit unions such as Portsmouth Savers in the region and others nationally are pioneering the development of products new to the credit union movement. These include a bank-style current account with cashcards and Cash Individual Savings Accounts. Brighton and Hove Credit Union is developing a range of differentiated loan products. Both of these credit unions have moved from traditional credit union products to develop new services designed around their clients' needs and wants. Their successes in growing credit union membership, (to almost 4,000 in the case of Portsmouth Savers) show that client-centred innovation can lead to success in tackling financial exclusion. It is difficult for smaller credit unions to innovate, but co-operation through ABCUL could ensure roll-out of new services in smaller financial inclusion providers across the region.

Home contents insurance is one of the financial products from which a substantial number of households (9.9%) are excluded. The National Housing Federation has prioritised financial inclusion as one of its five policy themes. It is working on the provision of a low or no-cost home contents insurance service for its members' tenants. By including the National Housing Federation in its high level regional group for financial inclusion, SEEDA can ensure that the benefits of this proposal are fully realised in the South-East.

South Coast Moneyline is pioneering a home improvements loan product in partnership with Portsmouth City Council, Brighton & Hove City Council, Eastleigh Borough Council, Chichester District Council and Gosport Borough Council. The Partnership has launched a new Home Improvement Loans Service to provide low cost loans to assist home owners to finance essential works to their properties. The loans are aimed at home-owners on low incomes or in receipt of means-tested benefits. Innovators should be supported and encouraged to develop their new services to a stage where they can be provided on a regional basis.

As outlined above, there is a gap for a micro-small business loan product across the whole region. This loan would average £20,000 and could be provided by a partnership between the six existing providers.

GROUP OR COMMUNITY GAPS

In terms of products, there is a notable absence, with the exception of the Fredericks Foundation, of specially targeted provision or marketing effort. No specialised marketing or product design is used to reach the particular sectors that the Government and SEEDA have been keen to help into the labour market. These include products targeted on women, ethnic minorities, recent migrants and people with disabilities. These loan products need not necessarily be self contained funds for these groups. Work by Prince's Trust funded by the Phoenix Fund on increasing participation by young women in their programmes has shown that large scale programmes can increase their outreach to specific groups by distinctive marketing approaches.

8. SUSTAINABILTY

WHAT IS SUSTAINABILITY

In terms of tackling financial exclusion, sustainability can be defined as the extent to which interventions can be maintained by structures and institutions. CDFI's and credit unions are social enterprises, balancing their mission and their business activities. They maintain a balance or a creative tension between running an efficient enterprise and staying true to their social goals. Within that broad view of the sustainability of financial inclusion service providers, we can distinguish three different types of sustainability;

Operational Sustainability: the extent to which the organisation can pay for its operating costs out of earned income (for example from interest income)

Mission-Driven Sustainability: the extent to which the organisation can raise money from government or other stakeholders by demonstrating social impact

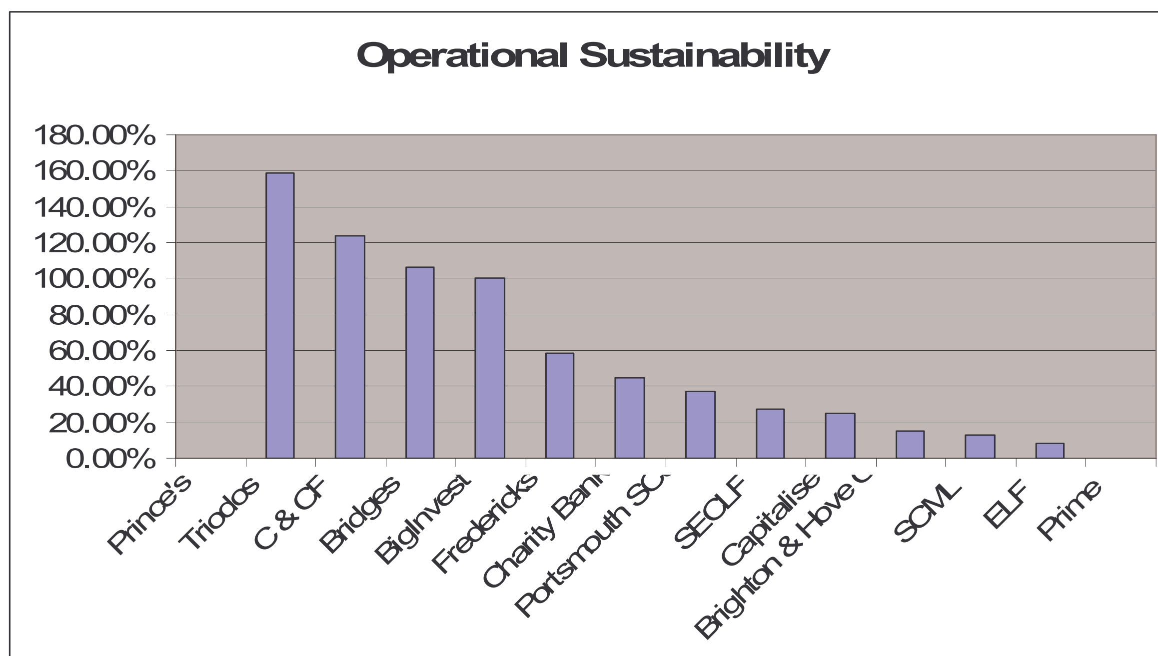
Structural Sustainability: the extent to which the organisation can raise money to pay for the cost of operations because of its structure (e.g. through fund raising or cross subsidy from a more profitable venture)

Many CDFIs and Credit Unions use a mixture of these three sources of revenue in order to balance their books. The three approaches are described in more detail below.

OPERATIONAL SUSTAINABILITY

Operational sustainability is achieved if a CDFI or Credit Union can cover its operational expenses from its income generated, normally from the interest income gained from its loan portfolio. The Operational Sustainability Ratio is the percentage of operating costs covered by earned income. Of those CDFI's which reported the ratio in the CDFA's *Inside Out* survey 2005, average operational sustainability was 36.1% although this covered a wide range from a low of 0.22% to 123%. Nearly half of CDFI's who reported had ratios of less than 20%.

Of the twelve CDFI's and two large CU's operating in the South East, operational sustainability ratios were obtained for thirteen (excluding Princes Trust). They ranged from 0% for Prime, which under its funding agreement, nets off all interest earned against revenue grant received to 158% for Triodos. Four of the CDFI's achieved full operational sustainability; Triodos, Co-operative and Community Finance, Bridges Community Ventures and BIGInvest. Three of these are social finance organisations and the fourth is a national community venture capital fund. Of the remaining organisations, sustainability levels ranges from 8.6% for Enterprise Loan Fund to 58.3% for Fredericks Foundation.



The pattern is of one community venture capital and four social enterprise lenders who are either fully operationally sustainable or are well on track to reach operational sustainability following a well-developed business strategy. Then there are five CDFI's and one Credit Union with portfolios' outstanding of over £300,000 and operational sustainability levels of between 20% and 60%. The graph shows a further nine organisations which were able to supply information, with portfolios outstanding of less than £300,000 and operational sustainability levels below 20% or unavailable but unlikely to reach higher levels.

The conclusion is that social enterprise lending, usually carried out at super-regional levels, is a sustainable operation based on large average loan sizes, relatively long loan terms and traditionally low write-off rates. Neither enterprise lenders nor personal lenders have achieved more than 60% operational sustainability and that figure was achieved, not from loan income but from commercial and charitable activities (Fredericks Foundation). The highest levels achieved in terms of loan interest income are just under 40% (Portsmouth Savers CU).

MISSION-DRIVEN SUSTAINABILITY

Mission driven sustainability is similar in concept to Social Return on Investment (SROI). SROI attempts to quantify the social returns of intervention by monetarising all of the values of benefits and disbenefits. SROI values of more than one achieved by a project suggest that there is a public interest to intervene. For financial intermediaries such as CDFIs and Credit Unions a lower operational sustainability may well be justified because their lending operations are achieving high social returns. The problem is that the departmentalised nature of national, regional and local government means that the savings are achieved across a broad front of the public sector, few parts of which see their role as being to support CDFIs even where their housing estate, health costs, benefit claims or tax revenues would all be improved by so doing.

An example would be in micro lending for self employment where the result of the loan is that someone formerly on benefits has become self employed. Not only is there a saving to the public purse from benefits payments but there will also be positive tax revenues. One way to evaluate this

is to assess mission-driven sustainability which in the case of CDFIs and Credit Unions is the extent to which the third-sector lender is able to reach and work with the most financially-excluded clients.

The main measurement tool used in relation to these organisations is average loan size as a percentage of GVA per head in the region. The rationale behind this internationally accepted metric is that poorer clients require smaller loan sizes, so it operates as a proxy for depth of market penetration to reach and work with the most financially excluded. Using GVA allows us to standardise the measure relative to regional wealth.

Organisation	Av. Loan Size/ GVA per head
Triodos	2241.34%
Bridges	1869.98%
BIGInvest	1254.80%
Charity Bank	376.44%
SECLF	358.51%
C & CF	129.07%
Capitalise	40.33%
ELF	22.38%
Prime	22.18%
Fredericks	14.87%
Prince's	10.04%
Isle of Wight CU	5.38%
S'hampton CU	4.95%
SCML	4.90%
P'mouth CU	3.48%
Bedford CU	3.23%
Isle of Thanet CU	2.72%
Amicus	2.69%
Hastings & CU	2.57%

The table above shows that the Credit Unions and South Coast Money Line work with the most financially excluded clients, with ratios of 5% and below. By international standards, this is a significant achievement in terms of reaching extremely financially excluded people. The enterprise lenders also achieve significant levels of market penetration ranging from 10% for Prince's Trust up to 40% for Capitalise. Internationally, ratios below 100% are regarded as successful in terms of depth of market penetration.

Defining, measuring and evaluating outputs, outcomes and impact is a weakness among some third-sector lending organisations, many of whom are still relatively young. It was intended to assess the percentage of clients based in the most deprived Super Output Areas in the Region, as an addition to the analysis above. However, too few of the organisations were in a position to provide that information.

Funders obviously need to balance scale and impact of operation with mission-driven sustainability, but the third sector lenders shown above can make the case that they are successfully reaching and working with their target market of financially excluded people and entrepreneurs. However, CDFI's and Credit Unions are not currently able to make claims for the social returns accruing from investments in CDFI's and Credit Unions because no solidly-based analytical model for measuring social return has yet been produced. This would be a ground-breaking piece of research that would

enable investment in CDFI's and Credit Unions to be carried out on the basis of evidence rather than hypothesis. We see an essential task for the High Level Group on Financial Inclusion to actively pursue the development of an analytical framework and a funding model. A very practical application of the framework would be a pilot research project between a CDFI or Credit Union and a Housing Association to investigate how the expansion of financial services to social housing tenants impacts on housing association costs and delivers social benefits. Given the National Housing Federation's commitment to financial inclusion, they might be willing to facilitate such a research partnership.

STRUCTURAL SUSTAINABILITY

An organisation can have operational and mission driven sustainability of below 100% and yet be sustainable if it can work out an alternative way of generating income or other forms of support to support its operating costs. This approach can be termed structural sustainability.

Third sector lenders use a variety of different business models to deliver financial services. Larger organisations and particularly social enterprise lenders making larger loans can afford to carry the overhead of a dedicated back-office operation and of general administration. This cost burden is far harder for smaller organisations to carry, particularly as smaller loans usually indicate more financially excluded clients who require more support to get through their loan. Some organisations including the Prince's Trust, Fredericks Foundation and Capitalise Business Support have developed different models of operation to improve their structural sustainability, which are outlined the in the main Supply-Side Report.

9. SUSTAINABILITY MODELS AND THE SUSTAINABILITY GAP

The terms of reference for the study included the requirement to assess the actual and potential sustainability of CDFI's and Credit Unions in the Region.

SOCIAL ENTERPRISE MODEL

The Supply-Side Report shows a model of social enterprise lending that can comfortably reach sustainability. The model shows that a lender with just over 40 loans outstanding with an average loan balance of £50,000 can be run with one full-time lender and one part-time administrator. It can cover its employment and operating costs and loan losses at 2% of the portfolio outstanding and produce a small operating surplus.

Most social enterprise lenders are operating at national scale, even when like LIF they run regional funds, and can expect to surpass this level of lending. Social enterprise lenders may need seed-corn support to get off the ground or to expand their operations into new regions, but the model is sustainable.

The only proviso relates to the need for business advice and training services for their clients, many of whom may require this support in order to reach investment-readiness. However, social enterprise business support is outside the remit of this study.

SMALL BUSINESS MODEL

A regional lending operation providing large micro or very small business loans (£7,500 - £20,000), whether run by one of the existing Enterprise CDFI's or as a partnership between them, can also reach sustainability. The SEEDA Demand-Side Report estimated that there was the potential to make 292 loans in this market segment across the South-East every year. The sustainability model in the Supply-Side Report is based on 165 loans outstanding, which given an average loan term of 4 years, would only require only just over 30 loans per year to reach sustainability. Providing this service through existing organisation, utilising their staff and resources would enhance the sustainability of those organisations.

MICROFINANCE MODEL

It has not been possible to produce a standalone microfinance model that will reach sustainability. The model is constrained by:

- The number of clients that a loan officer can handle, given the extra support need in the application process and in terms of follow-on support to complete the loan;
- Acceptable interest rates. Doorstep lending rates averaging 177% cannot be justified, as has been confirmed in the initial findings of the Competition Commission inquiry on the supply of home credit. Current microfinance rates average 14% and write-off rates average 8%, giving a portfolio yield of 6%. Assuming that loan losses remain steady, two loan officers are employed and they handle a maximum of 100 clients each, the CDFI would need to generate a net portfolio yield of 25% and therefore charge 33% on its loans to break even

The highest level that an efficient, stand-alone microfinance organisation can reach is to cover 60-80% of operational costs. This gap will remain even if current providers scale up and come much closer to meeting the coverage gaps in the Region. There are three main options open to providers:

- CDFI's can raise their average loan sizes and terms by expanding upwards into large micro-enterprise and very small business lending. In order to achieve regional coverage and equality of access for entrepreneurs, this would best be achieved through co-operation;
- CDFI's can spread their fixed costs across a broader base by developing other services, as South Coast Money Line is doing with its home improvement loans, by bidding for business support contracts or by diversifying into other areas of work as the Fredericks Foundation is doing;
- CDFI's can operate as part of larger business support agencies as Capitalise and Enterprise Loan Fund do, with a subsidiary structure to support transparency of financial and performance reporting .

Over the next five years, CDFI's should aim to achieve 60% operational sustainability on the basis of the lending operations. This will ensure that they remain focused on meeting client needs and satisfying unmet demand. In the longer term, ongoing subsidy of operating costs will only be possible if CDFI's can convince their stakeholders of their mission-driven sustainability – that they are reaching the parts of financial exclusion that no other provider can meet and that their social impact is transparent and valuable.

PERSONAL LENDING MODEL

The personal lending models in the Supply-Side Report can be applied to Credit Unions or CDFI's as it ignores the cost of capital, which has been the difference between the two organisations. Credit Unions traditionally captured members' savings on which they paid a dividend and onlent them. CDFI's either received capital grants for onlending or borrowed funds through Community Investment Tax Relief. Although the governance and control differences between the two types of organisations remain, the way in which larger and more successful Credit Unions operate is now closer to the CDFI model, as they receive revenue and capital grants and use CITR wholesalers to access funds. However, two version of the model have been presented, one for Credit Unions and one for CDFI's. Both can reach sustainability with 5 staff and 2,500 loans outstanding averaging £800 each.

Credit Unions and personal lending CDFI's can achieve sustainability but only by focusing on substantial growth. Portsmouth Savers has demonstrated that this level of growth can be achieved in more populated areas. Beacon CDFI's could be encouraged to develop to serve 5,000+ members in the following areas:

- Portsmouth, Southampton and Hampshire (Urban Hampshire Diamond for Growth)
- West Sussex including Horsham and Crawley (The Gatwick Diamond)
- Brighton, Hove and East Sussex (Brighton and Hove Diamond for Growth)
- Kent, including Thanet, Medway, Canterbury and Maidstone (Medway Diamond for Growth)
- Surrey including Guildford and Woking (London Fringe)
- Slough and Berkshire (Western Corridor)
- Milton Keynes and Oxford (Milton Keynes Diamond for Growth)

An innovative franchising model could be developed in the South-East to help serve the financially excluded in smaller, less densely populated or more rural areas. This could involve Credit Union volunteers carrying out local outreach and working as Directors and Credit Committee members for a local credit union with all of the back-office, support and marketing operations being carried out by one of the Beacon Credit Unions at a reasonable cost. With good IT support, this solution could combine the benefits of local, on-the-ground knowledge and commitment with the experience and expertise of professional credit union staff.

10. RECOMMENDATIONS

These studies have mapped financial exclusion, researched who the financially excluded are, reviewed the policy framework, assessed the coverage gaps left by CDFI's and Credit Unions, assessed their sustainability and now proposes a coherent set of recommendations.

Some Credit Unions and CDFI's in the South-East have demonstrated the potential to tackle the problems of personal and enterprise financial exclusion in the Region. However, this study has provided an opportunity to review and clarify the scale of the challenge facing them if they are serious about addressing financial exclusion. They need to raise their game substantially if they are to be treated as a serious option in the provision of affordable financial inclusion services.

SEEDA may recognise that CDFI's and Credit Unions work in very difficult circumstances, spanning the boundaries between community development and financial services and reaching communities that other approaches cannot touch. They are innovative and challenging organisations and play a significant role in investing sustainably in local communities. They have advantages over project-funded solutions because of their longevity, their ability to leverage and combine capital from the private sector and the third sector. Most of all, efficient and effective CDFI's and Credit Unions that have grown to scale offer long term sustainability because of the capacity to recycle investment.

Financial inclusion services, covering personal finance, microfinance and social enterprise finance, can make a significant contribution to the economic and social development of the Region, as a central element in SEEDA's economic inclusion work.

RECOMMENDATION 1: FINANCIAL INCLUSION STRATEGY

It is recommended that SEEDA should use its influencing role to form a high level group in the region to develop a Financial Inclusion Strategy for the Region, to sponsor strategic solutions to financial exclusion and exploring new ways of bringing private sector finance into growing the sector. This group could bring together the National Housing Federation and the major housing associations, local authorities and banks as well as representatives of CDFI's, Credit Unions and Citizen's Advice Bureaux.

RECOMMENDATION 2: MEASURING SOCIAL IMPACT IN FINANCIAL INCLUSION

SEEDA should sponsor the development of a solidly based analytical framework for measuring social return from financial inclusion work. A practical application of the framework would be a pilot research project between a CDFI or Credit Union and a Housing Association to investigate how the expansion of financial services to social housing tenants impacts on housing association costs and delivers social benefits to housing associations and the public sector. Given the National Housing Federation's commitment to financial inclusion, they might be willing to facilitate such a research partnership.

RECOMMENDATION 3: REGIONAL FUNDING AND SUPPORT FRAMEWORK

As part of the regional Financial Inclusion Strategy, SEEDA can play a central role in developing a regional funding framework covering the period of the Regional Economic Strategy, with initial commitments over a three year period. This could take advantage of the legacy funds, the Financial Inclusion Fund, the Local Enterprise Growth Initiative and European funding (ESF, ERDF and the European Investment Fund's JEREMIE Initiative) as well as SEEDA's own Single Pot resources.

In the short term, SEEDA and other funders should concentrate available resources to reward mission-driven lenders who are tackling financial exclusion efficiently and effectively, co-operating with other organisations, ambitious for scale and achieving increased financial sustainability in the sector. Phoenix Fund resources should be focused on support for existing CDFI's, particularly to enable development work to increase spatial coverage.

SEEDA could also ensure that regional Business Link advisors broker appropriate clients to CDFI's in the Region and that Enterprise Gateways work closely with the CDFI's in their areas.

RECOMMENDATION 4: BEACON CREDIT UNIONS / CDFI'S

It is recommended that personal financial exclusion should be tackled by encouraging Beacon Credit Unions or CDFI's to service 5,000+ members in the following areas:

- Portsmouth, Southampton and Hampshire (Urban Hampshire Diamond for Growth)
- West Sussex including Horsham and Crawley (The Gatwick Diamond)
- Brighton, Hove and East Sussex (Brighton and Hove Diamond for Growth)
- Kent, including Thanet, Medway, Canterbury and Maidstone (Medway Diamond for Growth)
- Surrey including Guildford and Woking (London Fringe)
- Slough and Berkshire (Western Corridor)
- Milton Keynes and Oxford (Milton Keynes Diamond for Growth)

An innovative franchising model could be developed in the South-East to help serve the financially excluded in smaller, less densely populated or more rural areas. This could involve Credit Union volunteers carrying out local outreach and working as Directors and Credit Committee members for a local credit union with all of the back-office, support and marketing operations being carried out by one of the Beacon Credit Unions at a reasonable cost. With good IT support, this solution could combine the benefits of local, on-the-ground knowledge and commitment with the experience and expertise of professional credit union staff.

RECOMMENDATION 5: EXPANSION OF ENTERPRISE FINANCIAL EXCLUSION SERVICES

Financially excluded areas which have no enterprise coverage for over 30's include Slough, Dover, Milton Keynes and Oxford. The areas with the greatest potential for enterprise development include Brighton and Hove, Wycombe, Milton Keynes, Aylesbury Vale, Windsor and Maidenhead, West Berkshire, Wealden, South Oxfordshire, Elmbridge, New Forest, Waverly, Wokingham, Medway and Guildford.

CDFI's should be encouraged to bid to provide microfinance services in these areas on the basis of service-level agreements, with contracts terminated for non-performance. They should also be required to produce regional offerings of products and services particularly targeted at the specialist sectors where SEEDA has been keen to overcome economic inactivity. These include services for women, ethnic minorities, recent migrants and people with disabilities, with opportunities for different organisations to take the lead for different target groups. Finally, CDFI's should be supported to offer a regional product targeted at large micro-businesses with an average loan size expected of £20,000. This will fill a gap in the market and increase CDFI sustainability.

RECOMMENDATION 6: MICROFINANCE AND OPERATIONAL SUSTAINABILITY TARGET

It is recommended that Micro-enterprise CDFI's, (lending to businesses with fewer than 10 employees) should aim to achieve 60% operational sustainability on the basis of their lending operations. There are three main options open to providers:

- CDFI's can raise their average loan sizes and terms by expanding upwards into large micro-enterprise and very small business lending. In order to achieve regional coverage and equality of access for entrepreneurs, this would best be achieved through co-operation;
- CDFI's can spread their fixed costs across a broader base by developing other services, as South Coast Money Line is doing with its home improvement loans, by bidding for business support contracts or by diversifying into other areas of work as the Fredericks Foundation is doing;
- CDFI's can operate as part of larger business support agencies as Capitalise and Enterprise Loan Fund do, with a subsidiary structure to support transparency of financial and performance reporting .

RECOMMENDATION 7: ONE POINT OF CONTACT

In order to achieve this co-ordinated approach to tackling enterprise financial exclusion in the South East, CDFI's should form a single, incorporated organisation that can act as a single point of contact for SEEDA and other regional organisations, can encourage co-ordination of activities and provide a conduit for finance for CDFI's in the Region.

The single point of contact could also develop a single, regional interface for referrals and marketing information to link with Business Link and Finance South East and establish a web portal so that anyone in the region can identify their local provider of enterprise financial services. It is possible that CDFI's might decide to develop shared back-office operations at a future date, to reduce costs.

RECOMMENDATION 8: COVERAGE AND PRODUCT GAPS

There is a notable absence of specially targeted provision or marketing effort for enterprise loans. No specialised marketing or product design is used to reach the particular sectors that the Government and SEEDA have been keen to help into the labour market. These include products targeted on women, ethnic minorities, recent migrants and people with disabilities. It is recommended that CDFI's work together to develop regional offerings with different organisations taking the lead to develop different specialisms.

The main product gap in the provision of enterprise financial inclusion services is in the gap between micro and small business lending. There is a gap in the market for loans between £7,500, which existing CDFI's are providing and £20,000 plus, which are provided by the South East Community Loan Fund, in disadvantaged areas. It is recommended that the market be served by a joint approach by all six enterprise CDFI's offering a standard loan product to businesses across the region. This would require both access to loan capital and the development of standard loan application and analysis processes.

Home contents insurance is one of the financial products from which a substantial number of households (9.9%) are excluded. The National Housing Federation has prioritised financial inclusion as one of its five policy themes. It is working on the provision of a low or no-cost home contents insurance service for its members' tenants. By including the National Housing Federation in its high level regional group for financial inclusion, SEEDA can ensure that the benefits of this proposal are fully realised in the South-East.

New product and service innovators should be supported and encouraged to develop their new services to a stage where they can be provided on a regional basis.

There is no gap in the provision of social enterprise finance in the Region, but that work is needed to develop confidence and skills in a relatively weak market. Rather than increasing grant aid directly to social enterprises or indirectly through finance providers, investment could be made in education and business support for the sector so that it becomes more ambitious and professional in its social enterprise operations.

RECOMMENDATION 9: WHOLESALE FUNDS FOR ONLENDING

All five of the large social enterprise lenders, BIGInvest, Charity Bank, ICOF, LIF and Triodos, are accredited by the Small Business Service to use Community Investment Tax Relief and can wholesale funds for onlending to other CDFI's. Wholesaling money in this way brings a private sector discipline to CDFI's and forces the development and transparency of financial and social reporting systems. While smaller CDFI's may require some capital grants in particular where they are extending their operations into new areas or products, it is important that neither grants nor soft loans damage this developing capital market for CDFI's.

CONCLUSION

Despite its great wealth, the South East of England has significant problems of financial exclusion that affect individuals, households and enterprises as well as the communities in which they are based. More than any region in the UK, the South-East of England is in a position to overcome the challenge of personal financial exclusion and to improve community cohesion and trust in deprived areas. Further, by mobilising the positive impacts of enterprise and social enterprise in deprived communities on a regional level, tackling financial exclusion among enterprises by improving their access to finance, the agency can increase employment, create multiplier effects and build supply chains, increase the tax base, improve the physical environment and enhance the availability of local services. Such an approach would also empower local people to use their own resources and capabilities to earn a living, build a business, provide employment for others and earn status and respect within those communities.