

# Debt and the Impact of the Rising Cost of Living: Evidence from the Credit Union Sector 2023

1. This short report will provide evidence for the Senedd's Equality and Social Justice Committee's inquiry on debt and the rising cost of living, from the perspective of the credit union sector. This report is submitted by the Association of British Credit Unions Limited (ABCUL), the primary trade body for credit unions in Britain, in representation of its Welsh member credit unions.
2. This report will provide the following information:
  - a. An overview of the Welsh credit union sector
  - b. Impacts of the cost of living crisis on personal debt as observed by credit unions
  - c. Suggested recommendations to be made to Welsh Government for the 2023-24 budget, to support the credit union sector's work during the cost of living crisis

## **Background: The Role of the Welsh Credit Union Sector**

3. Credit unions are financial cooperatives, that offer ethical, affordable and safe financial services. They primarily provide savings products, loans and financial education to their members. Individuals can join a credit union if they meet the credit union's membership criteria, a common bond usually defined as living in a certain area or working in certain industry. In 2022, credit unions in Wales provided financial services to 80,000 people, held £66m in assets, and had £24m out on loan to members.
4. The credit union sector plays a vital role for financial inclusion and building financial resilience in Wales. Credit unions provide low-cost and inclusive credit. The sector has historically offered credit to individuals that may be turned away from traditional banks, and have provided a safe and affordable alternative to high-cost lenders and loans sharks. Though they provide credit, credit unions also look to build individual's financial resilience through actively encouraging their members to save and adopt good money habits. They aim to turn borrowers in to savers, with many credit unions requiring their members to put away savings as part of a loan repayment.
5. In the cost of living crisis, credit unions are more important than ever in helping people with their financial wellbeing and building financial resilience on the ground. Credit unions are taking a range of steps over and above their normal work to support their member's financial wellbeing in the current economic circumstances. As well as providing their members with support and loan forbearance where needed, many credit unions are undertaking

charitable work and outreach initiatives to support their communities with the cost of living crisis.

## **Debt and the Cost of Living from the Perspective of Credit Unions**

6. This section will highlight the trends broadly seen by credit unions related to personal debt and the impact of the rising cost of living. Please note that the extent that these issues apply to a credit union will vary according to the characteristics of its common bond and membership base. However, the following trends have been identified by the majority of credit unions.
7. Increased demand for credit: there has been a general increase in loan applications to credit unions since the onset of the cost of living crisis. Credit unions broadly associate the increase in loan applications with the increased cost of living and decreased household disposable income, leading to an increased demand for credit to cover household expenditure. Whether credit is sought to cover essential or non-essential expenditure varies between loan applicants, but there has been an increase in the demand for credit to cover essential household expenditure. There is also a rise in individuals repeatedly applying for credit.
8. Increased demand for small-sum emergency loans: credit unions are seeing a new demand for small-sum emergency loans from individuals, to cover essential living expenses in the short-term. Small-sum emergency loans have commonly been requested to pay for a weekly food shop, from individuals in financial crisis with no ability to pay for food.
9. Increase in declined loan applications: the cost of living crisis is reducing access to credit for many individuals due to a drastic decline in their ability to afford to repay a loan. Credit unions are responsible lenders and will decline a loan application according to its risk appetite, particularly where it is clear that a loan will cause an individual further financial difficulty in future. The increased cost of living is significantly decreasing the ability of individuals to afford credit, leading to a notable increase in the rate that credit unions are declining loan applications. This trend is seen across income brackets, with some credit unions noting that the largest decrease in affordability is observed with middle-income earners, who would have previously been able to afford credit without issue.
10. Increase of pre-existing debt of loan applicants: credit unions are seeing a rise in loan applications where the individual has pre-existing debt with other providers of credit, often having reached their limits on credit cards and other forms of credit. There is also a significant increase in applications where the debtor is in arrears with their utility bills. Some credit unions are seeing a rise in individuals applying for debt consolidation loans.

11. Debtors are struggling to repay their debts: credit unions are generally experiencing an increase in missed loan payments. There has also been an increase in credit union members seeking loan forbearance, such as reduced loan payments. In line with the increase in debtor's struggling to repay their debt, credit unions are experiencing an increased frequency of members entering insolvency solutions, particularly Individual Voluntary Arrangements (IVAs).

### **Recommendations for the Welsh Government's Draft Budget 2023-24 Relating to the Rising Cost of Living and Personal Debt**

12. This section will identify potential recommendations to be made for Welsh Government's Draft Budget 2023-24 for addressing issues of debt during the cost of living crisis, in respect of the credit union sector.
13. The credit union sector acknowledges the continued and invaluable support of Welsh Government has already provided for the credit unions. Welsh Government has a strong record of recognising the value of credit unions in supporting financial wellbeing and the unique challenges the sector faces. Welsh Government's Credit Union Grant Programme for 2023-26 will offer credit unions the investment to undertake projects outside their day-to-day business, that will expand their reach and support the development of the sector. In addition, the loan expansion scheme in 2022 has enabled credit unions to offer access to credit, with credit unions noting that the Programme has enabled them to overcome their credit risk appetite, to provide access to a safe and affordable source of credit to those that have nowhere else to turn.
14. However, there are a number of challenges the credit union sector and its members are facing due the current economic circumstances. In light of this, there are further measures that Welsh Government could consider to support the credit union sector's work during the cost of living crisis. This report suggests the two following recommendations are made to Welsh Government for its 2023-24 budget:
  - a. Extension of the loan expansion scheme to different types of credit
  - b. Funding to support credit union's operational delivery in the context of high inflation
15. The first recommendation for the Welsh Government budget is for the extension of loan expansion scheme to guarantee different types of lending. Credit unions have already received support from Welsh Government in 2022 to guarantee small-to-medium loans for new members of the credit union. This support has provided invaluable support in allowing credit unions to exceed their credit risk appetite and provide access to affordable credit to those that would otherwise have turned to high-cost or illegal money lenders. However, there is opportunity to continue and develop this scheme, by

providing funding to cover different types of credit in the cost of living crisis. As this report notes, there is a growing demand for small-sum emergency loans to cover the cost of essentials in the short-term. Funding to cover small-sum emergency loans could support credit unions with helping more people in financial crisis, where these loans are outside the credit union's normal credit risk but still appropriate for that individual. Whilst small-sum emergency loans will not be a long-term solution to the rising cost of living, they can offer individuals in financial crisis a lifeline, as well as preventing individuals from approaching loan sharks in desperation. Funding to cover small-sum emergency loans could be used to compliment other cost of living support measures from Welsh and UK Government.

16. The second recommendation we would make is for Welsh Government to support credit unions with increased operational costs. Credit unions, like their members, are facing increased costs, due to inflation of operating expenses. However, credit unions are also facing increased costs in the cost of living crisis due to increased forbearance on loans to members, loan delinquency and insolvencies.
17. On top of the financial strain credit unions are under from increased costs, the rising cost of living is fuelling a demand for higher wages from the labour market. Many credit unions report that they are facing significant challenge recruiting and retaining staff due to the pressure to delivering higher wages. Credit unions operate on a not-for-profit basis, and therefore struggle to substantially increase staff wages, especially whilst facing increased overheads more generally. Recruiting and retaining staff is integral to the operations of the credit union. As a result, this challenge poses long-term structural risk to the credit union sector's ability to deliver it's affordable and inclusive financial services. It is recommended that the Welsh Government consider the potential for financial support for the credit union sector to overcome the operational challenges presented by high inflation.
18. Furthermore, it is recommended that Welsh Government holds a roundtable discussion to directly engage with credit unions on the rising cost of living. This would provide the opportunity to discuss issues the sector is facing during the cost of living crisis, the impacts of the cost of living crisis that credit unions are seeing on the ground, and potential policy solutions to promote financial wellbeing at this time.