



# Creating Effective Partnerships to Support Financial Inclusion

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and Zara Ransley

September 2019

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Our team has a wealth of specialist knowledge and skills across the public and private sector and we provide services and advice to researchers, funders and policymakers.

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# Creating Effective Partnerships to Support Financial Inclusion

A report on the issues and opportunities for social and community lenders and fintech collaboration to support financial inclusion in the United Kingdom

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# Foreword

**Innovation takes many forms. Often when we think of innovation we think of new technologies and certainly innovation in fintech (financial technology) has changed the face of the finance industry over the last decade. There is now a plethora of new products and solutions that are supporting better financial life for British consumers, from challenger banks to income smoothing products. From budgeting tools to new credit scoring mechanisms fintech has brought a sea change as to how we manage our money and financial transactions, but like many technological transformations those who need them the most often get left behind.**

We at Nesta see a different type of innovation is possible. We believe that innovation in the sector won't only include the technology that is being developed but also the innovative partnerships that can emerge.

This rapid research report was commissioned by Nesta to help us understand better the possibilities and challenges that collaboration between fintech companies and affordable credit providers could bring. Is it possible to harness the skills and expertise of the community lending sector and those of the fintech sector to make better and more ethical products and services for more consumers?

The team at MyPocketSkill worked to develop this report and we are grateful to Matthew Harker and Zara Ransley for their hard work and to the interviewees for giving their time so generously.

We hope this report can be used by others thinking about and trying to harness the skills and resources of fintechs, and those of the community lending sector, and we hope others will build on this research.

At Nesta we run a variety of practical programmes and challenges that partner across sectors and we will continue to share our learning about partnership and how to successfully make it happen.

We expect that, for a true transformation of the sector and to deliver better services for those excluded from the financial system, there will need to be a variety of changes including: new and better legislation and regulation; more support for the current community lending sector; new ethical challenger solutions; encouraging current fintech providers to offer financial inclusion products and services, and of course we will need to support charities, communities and other 'people powered' solutions to ensure all are included.

**Kate Sutton**

September 2019

# Executive summary

## Introduction and context

How can fintechs form effective partnerships with social and community lenders to support financial inclusion and what are the key issues and opportunities facing potential collaboration?

This rapid report introduces a set of primary and secondary research and insight, to better understand and categorise the landscape, and explore opportunities for better cross-sectoral collaboration between social/community lenders and fintechs to support financial inclusion.

Although there are pockets of good practice, the fintech sector has not yet engaged with credit unions (CUs) and community development financial institutions (CDFIs) at scale and, overall, challenges exist in applying disruptive technologies in ways that improve the lives of those who are excluded from the current system.

This work researches and documents the issues and potential solutions underpinning the narrative of financial inclusion. The focus here is to bridge the gap between digital providers of financial services (fintechs) and social and community organisations working with financially excluded groups.

## An assessment of readiness – CUs/CDFIs and fintechs

Our research highlights many strengths of these organisations. Beyond their badge of being fair, flexible and ethical, these organisations have a rich knowledge of their customer base and often a wealth of historic data, mapping out members' preferences and behaviours. These organisations tend to offer a personalised, customer-centric approach and their offer itself often represents good value, particularly where the default option is the doorstep lender or the top company on the search engine results.

However, there are also issues in CUs/CDFIs' ability to grow and engage effectively with technology:

- Despite sector consolidation, many organisations are subscale, which can lead to issues around capabilities, promotional reach and unit economics.
- Legacy system and business processes often constrain their ability to respond to customer needs, particularly in respect to time to respond (e.g. time taken from initial click to loan acceptance).
- Structural constraints (e.g. where credit unions have specific capital and interest rate constraints, which potentially have unintended consequences for their competitiveness).
- Lingering public perception issues ('credit unions are just for poor people').

Fintech companies, using technologies to widen the access of consumers and businesses to new financial products and services, are already playing a part in this sector. For example, we are already seeing novel approaches to assessment and credit scoring, payment profiling to suit unpredictable earnings, and open banking integration. We identified six areas where technology can potentially have a significant impact on CUs/CDFIs' ability to grow:

1. **Frictionless workflow:** The creation of products with more streamlined workflow (e.g. to allow faster decision-making).
2. **Customer/member acquisition and management:** Digital marketing, segmentation, brand building, search optimisation and CRM functions.
3. **Scalable solutions:** Approaches which will lower the unit cost of execution (e.g. shared platform or blockchain/distributed-ledger-technology-based systems).
4. **Digital experience (UI/UX):** Overall customer experience (UI/UX). Offering greater immediacy, personalisation and customer experience.
5. **Integration:** Ability to integrate better into customers' own finances or to other third-party systems.
6. **Analytics/AI/data science:** Data analytics and decision support, machine learning, chatbots/interfaces and online verification/security.

## Overcoming potential blocks to partnership

For CUs/CDFIs three principal blocks to effective partnerships are around organisation capability, effective partner selection and perceptions of past failures:

**Organisational capacity** – Unable to engage effectively because of lack of resource or client-side tech expertise. Here, potential partnerships could focus initially on larger organisations as exemplars (with a cohort of fast followers) or enable consortia of smaller CUs or engage in upskilling/development programmes alongside implementation. Joint ventures might be one way of achieving this.

**Partner selection** – Because resource and expertise are scarce commodities, CUs/CDFIs can find it difficult to evaluate which fintech to work with; there may be concerns, for example, about the organisational stability of a potential partner. An area of potential assistance is therefore due diligence, for example to help establish criteria or a framework of capable suppliers.

**Culture and perceptions of past failures** – Many CUs are culturally risk averse and unwilling to jeopardise current operational processes. There is nervousness about wasting time on initiatives that have not worked in the past. In any new technology initiative, project coordinators will need to be clear about how it is going to be different this time. Success factors based on learning from previous attempts include delivering initiatives that are more user-designed, less top-down, modular rather than big bang and delivering quick wins through an agile approach.

There are also potential blocks from fintechs' perspective. For fintechs, these blocks involve customer capability, sector knowledge and strategic importance:

**Readiness:** Fintechs currently struggle with CU/CDFI customers who are not ready or willing to embrace change, which may involve changes to business processes not just new technology. One way of addressing this is through case studies of current good practice and generating buy-in for a vision/roadmap for the sector.

**Sector knowledge:** The technical capabilities exist in the fintech community but the CU/CDFI landscape is alien to all but a few sector specialists. Briefing sessions and matchmaking within the fintech community to stimulate those with relevant transferable technologies could be a way to address this.

**Need for a CU/CDFI partner?:** Some fintechs that we spoke with already have a proposition for financially excluded customers and do not see value in partnership. Here, there may be a need to better articulate the win-win aspects of the challenge, for example in the context of the global opportunity or in opening to a broader customer base (e.g. local government/NHS employees) and access to data and experience.

# 1. Introduction and objectives?

**With eight million people struggling to keep up with bill payments and credit commitments,<sup>1</sup> and more than 5.4 million loans made in the 12 months to June 2018 in the high-cost, short-term loans sector,<sup>2</sup> it is clear that a significant proportion of the UK population is locked-out of mainstream lending and turning to high-cost credit.**

**This is a mainstream problem looking for a mainstream solution.**

Social and community lenders, principally credit unions (CUs) and community development financial institutions (CDFIs), represent a valuable resource in the battle against financial exclusion. But, with a relatively low market share, they can struggle to break into mainstream recognition and currently many of these organisations remain underpromoted and underpowered.

Conversely, with unprecedented growth and investment, for example benefitting from £2.6 billion of investment since early 2018,<sup>3</sup> the UK fintech sector potentially offers new perspectives on this problem, and from this pool of digital innovation expertise, there may be opportunities to leverage the technologies and toolsets of this sector to good effect. However, while there are a few fintechs which are actively working to target these customers and work collaboratively with social and community lenders, it is currently not clear whether there is enough common ground between these two types of organisations in terms of understanding, aims and interests, to work collaboratively.

This report looks at a set of primary and secondary research and insight, to better understand and categorise the landscape and explore opportunities for better cross-sectoral collaboration between social and community lenders and fintechs to support financial inclusion.

## 1.1 Context

The roots of financial exclusion are complex, with many often-overlapping risk factors involved. These factors relate to who you are, your financial circumstances and where you live; with age, ethnicity, gender, personal and household income, employment, health status and geographic location all playing a major part. For example, those on low income with less education, part of a BAME community or with a migrant background and either very old or very young are more likely to be financially excluded than others. Also, women are more likely to be excluded from financial services than men, and households with no wage earner are more likely to be completely financially excluded. Other groups with a higher propensity to financial exclusion include people who are single parents/single people with no children, students and unemployed individuals, those with disabilities and those living in rural areas.

The impact of financial exclusion also plays out in different ways across these different segments. The most prevalent issue for consumers is dealing with debt. An estimated nine million adults borrow money to buy food or pay their bills, equating to 17 per cent of the



adult population, and this is correlated with overall wellness; the more people rely on credit for everyday spending, the less satisfied they are with life in general.<sup>4</sup>

From an end-customer perspective, expectations are increasingly fuelled by their overall experience of digital services. Mobile apps have simple, slick, intuitive interfaces with immediate responses and compelling design. These expectations spill over into customers' expectations of digital financial services; users want access to immediate and intuitive solutions to solve credit issues. It is therefore no surprise that some of the most profitable commercial lenders then, are also the ones offering newer digital technologies to achieve a wide customer reach, an immediacy of response and industry-disrupting innovation.

The landscape is mixed. Social and community lenders, principally credit unions (CUs) and community development financial institutions (CDFIs), exist to provide fair and equitable financial services to the communities they serve (typically a geographic, faith or employment base of individual and business members):

- **Credit unions:** 420+ organisations which have more than 1.8 million adult members, a loan book of some £1.6 billion<sup>5</sup> and lending c. £700 million a year.
- **Community development financial institutions (CDFIs):** Social enterprises whose mission is to deliver responsible, affordable lending to help individuals, businesses, social entrepreneurs and communities who struggle to access finance from mainstream banks. In 2018, around 50 CDFIs lent c. £250 million.<sup>6</sup>

However, this is still relatively modest within a sector which, for example, currently lends more than £5 billion a year in high-cost loans.<sup>7</sup> Although there are pockets of good practice, the fintech sector has not yet engaged with this sector at scale and overall, there appears to be a challenge in bridging the gulf between these two types of organisations and in applying disruptive technologies in ways which improve the opportunities for those most at risk of exclusion.

## 1.2 Overview and objectives

This work researches and documents the issues and potential solutions underpinning the narrative of financial inclusion. The focus here is to bridge the gap between new digital providers of financial services ('fintechs') and social and community organisations working with financially excluded groups, and focuses on questions around:

- What are the categories of individual who are at risk of financial exclusion?
- What are the trigger events for each of these categories in terms of the risk being realised?
- What are the support gaps in enhancing financial inclusion for those at risk?
- And considering respective capabilities, what are the opportunities for sector providers to partner more effectively in widening inclusion?

In compiling this report, we have undertaken a combination of desk research, from previous studies, research and related literature, combined with stakeholder engagement, across a cross-section of the sector. The findings of this work then provide a snapshot of the current dynamics, issues and challenges of financial inclusion, relevant to creating improved partnerships in this sector.

## 2. Financial inclusion: Where are the gaps?

Effective partnerships are dependent on shared understandings and appropriately aligned objectives; we therefore wanted to understand how providers would respond to various gaps in financial inclusion and whether there was a common understanding of the characteristics of those individuals who are at higher risk of being financially excluded and the trigger events which then often lead to that exclusion.

### 2.1 A persona-based approach

Our starting point was a set of personas that describe some of these common types of exclusion. We have developed these from secondary research, with many of the sources used directly drawing on the experiences of those at risk of financial exclusion. The personas do not attempt to provide a comprehensive picture of all types of exclusion, but rather, highlight some typical examples, using a relatable, narrative approach, describing the core characteristics of the persona, their lifestyle and vulnerabilities, as well as the specific trigger points in relation to risk.

Based on these personas, we have highlighted some of the current issues and gaps for those individuals overleaf, in **Figure 1**, and a fuller description is included in **Appendix 1**.

Figure 1: Financial exclusion – personas, issues, triggers and needs

Persona	Key issues	Potential triggers	Needs a quick decision	Needs awareness of lower-cost alternatives	Needs help to navigate the system	Needs help to rebuild credit history	Needs to build financial capability	Needs cushioning against financial shock	Needs flexibility, e.g. on payment/terms	Needs simple, intuitive mobile-friendly interface
<b>Gaëlle</b> (student, part-time worker)	No consistent employer or work patterns. No credit history. No savings.	Work dries up. Financial shocks (sudden large bill, or loss). No awareness of affordable credit lines, so borrowing more likely to result in indebtedness.	X	X			X	X	X	X
<b>Harry</b> (worker, previous debt, mental health issues)	Past issues/ credit history compromises his ability to borrow.	Potential mental health issues related to stress around finances. Financial shock (no savings, so not well insulated against shock).	X	X		X	X	X		X
<b>Cassie</b> (single mum, p/t employment)	Struggling with bills already. Uses high-cost short-term lending.	Loss of employment/ income. Lack of job security.	X	X			X	X	X	X
<b>Joan</b> (vulnerable, living alone, rural)	Financially excluded on the basis of digital skills, health and rurality.	Vulnerability as a consequence of deteriorating health. Unable to navigate the system to find effective alternatives.		X	X		X			

## 2.2 Notable issues and gaps in addressing these needs

The social and community lenders and fintechs we spoke with had a broad acceptance of the above personas and the issues that were leading them towards financial exclusion. Addressing the challenges of these personas and considering the current offer from providers in this sector, three specific gaps for these personas include:

- **Awareness of alternatives** – credit union CEOs highlighted the potential higher costs of the default option (the doorstep lender or the top commercial lender in the Google search).
- **Being able to easily source products** which are suitable for those without regular pay packets, and that do not rely on either good credit history or a regular current wage.
- **Lower-cost products which are simple**, intuitive, and come with an immediacy of decision, where customers are looking for a quick resolution. A recurrent theme from all that we spoke to was members/customers are managing their money on a week-by-week basis and an immediate resolution is more important than longer-term implications.

There are also challenges for these personas, which impact on the content and focus of appropriate digital and face-to-face offerings. A few of these include:

- Financial exclusion is often conceptualised as being a function of both financial capability (having the knowledge, skills and motivation to understand and use financial products) and the extent to which products suitable to an individual's needs are accessible.<sup>8</sup> The former is a factor for all of the above personas; for instance, where poor decision-making on competing financial products may be likely or where savings-behaviours are not widespread.
- Individuals like Joan, who are excluded based on rurality and digital literacy, are not comfortable using digital technology and have hitherto relied on face-to-face interaction. Here there is potentially a risk that new web/app-based solutions may serve to deepen the divide. We estimate that there are more than 1.6 million people like Joan (older people, 65+, who are struggling financially).<sup>9</sup>
- Many of the more innovative fintech providers are focusing on those who may have patchy credit histories but now have regular earnings. For example, by being able to deduct loan payments or pay earnings more promptly, directly from employers' payroll, companies like Neyber and Wagestream are effectively able to reduce the risk profile of the transaction and give less weight to credit history (see examples<sup>10</sup>). Therefore, these types of products may be useful for Harry, but less so the other three.

# 3. Responding to financial exclusion: Respective strengths and weaknesses

We also explored specific strengths and weaknesses of providers' capabilities, based on their own observations. Our conversations highlight several themes, summarised in Figure 2, which help to frame the issues and opportunities for CUs/CDFIs.

Figure 2: Advantages and weaknesses/Issues for social and community lenders

Advantages	Weaknesses/issues
<ul style="list-style-type: none"> <li>• Badge of being fair, flexible and ethical</li> <li>• Detailed customer knowledge and a wealth of historic data</li> <li>• Personalised, customer-centric approach</li> <li>• Overall value of their offer</li> </ul>	<ul style="list-style-type: none"> <li>• Subscale – leads to issues around capabilities, reach and unit economics</li> <li>• Timeliness of execution (systems)</li> <li>• For CUs – capital/APR constraints</li> <li>• Possible public perception issues ('CUs are just for poor people')</li> </ul>

## 3.1 How does the social and community lender sector differentiate?

One of the key potential differentiators for these organisations is their perceived status as fair, flexible and ethical lenders, typically with a member/community interest at heart and not profiting from indebtedness. This also translates into behaviours and incentives for both sides (CUs/CDFIs and members/customers) being well-aligned and resulting in high levels of customer satisfaction. However, it is also possible that this message is diluted through the use of terms 'fair', 'flexible' etc.) which often appear in commercial lenders' offers; therefore, this differentiator is potentially devalued through a lack of specificity, and with ambitions from new market entrants to democratise financial services (e.g. Monzo's mission: 'Monzo makes money work for everyone').

Players in this sector show a detailed knowledge of their customer base and could clearly articulate customer needs and motivations with reference to the personas that we shared. Many had access to useful sources of data around these customers (e.g. using data segmentation techniques) and have used this to build up a good understanding of members/communities relevant to their common bond.<sup>11</sup> For many that have been around for 20+ years, there is also a pool of rich historic demographic and performance data.

A hands-on, personalised approach by these lenders is also a differentiator; but this can be both a plus and a minus. It is positive in the sense that it offers a high degree of personalisation, relationship management and being able to meet with customers face-to-face, where it is difficult to decide based on data alone. Some CUs argued that the relationship is lost with automation, and that the ability to widen lending criteria or offer greater flexibility is achieved through deep knowledge of both customer and local economic circumstances, and that a strong relationship with those customers is achieved by long-term memberships rather than simply a one-off transactional loan.

Others seem to be moving away from this approach (one CU CEO told us: *"We don't interview any more, but we may ask supplementary questions by email."*) Nevertheless, customer satisfaction ratings for credit unions are very high; for example, a recent report indicated that 81 per cent of members were extremely/very satisfied and 84 per cent would recommend to a friend.<sup>12</sup>

Finally, the rates offered by credit unions are viewed in general as being favourable to many commercial lenders, particularly in consideration of the type of financially excluded customer, where commercial rates are often at the top-end of what is now permitted for high-cost, short-term loans by the FCA (i.e. no more than 0.8 per cent per day and to pay back no more than double the loan amount over the life of the repayment). For example, a commercial lender might apply a rate of 299 per cent APR for a loan of £1,000 for 12 months, whereas a CU would cap at 42.6 per cent. This is not necessarily true of CDFIs, where the same cap does not apply.

## 3.2 Issues/weaknesses for CUs/CDFIs

The most common theme is scale. All CUs that we spoke with highlighted issues that are either directly or indirectly a function of scale, including:

- **Reach** (e.g. inability to promote to a wider customer base)
- **Resource constraints** (e.g. lack of bandwidth to design or implement business process changes)
- **Capability constraints** (e.g. lack of technology capability, either to coordinate in-house changes or to vet external suppliers)
- **High unit costs** (e.g. harder to drive discounts for payment processing and credit scoring).

While we found examples of good practice and transformation, the overall technology base was recognised by many in this sector as being suboptimal. The consequences of this tech deficit are:

- Added resources needed through manual processes and double entry
- Limited ability to integrate with third party systems (loan portals, open banking, payroll)
- Limited ability to apply data insights (past performance to inform future decisions).

Another potentially more contentious issue relates to the slow-stream nature of the application process and the inability to make real-time decisions. Member/customer expectations are in-part fuelled by commercial brokers'/lenders' offers ('Get cash within 15 minutes'), but the inability to offer comparable latency (coupled in some cases with a lack of appetite to take on this type of customer) means that many applicants are defaulting to services that do offer instant results. A recurring theme in our conversations was that customers prized speed above cost.

Credit unions and CDFIs also raised structural and regulatory constraints as being problematic. Key points here relate to:

- The credit union interest ceiling, which they cannot exceed (currently 3 per cent a month, or 42.6 per cent APR<sup>13</sup>). The issue being that this potentially precludes certain types of high-risk, short term lending. In contrast, from CDFIs, where the ceiling does not apply, we saw examples of much higher rates (200 per cent+).
- Capital-to-asset ratios (for example, larger credit unions are required to maintain a 10 per cent capital-to-asset ratio).<sup>14</sup>
- CDFIs raised issues about constraints in accessing equity finance, with structures such as an asset lock in place.

One further challenge for credit unions stems from customer perceptions. Although we did not engage directly with end customers/members during this research, there is evidence from both the UK and overseas that credit unions have struggled with their clarity of message. Issues here include a perception that the CUs only serve the poor and that a CU/CDFI may be less safe than a bank. There are reported difficulties in customers grasping the 'member' concept and in associating credit unions with lower interest rates, with a quarter of members themselves not being aware of these two key points of differentiation.<sup>15</sup> Also, it is not clear that credit unions and CDFIs have a good understanding of the segments of the population who could potentially be members. Such findings have influenced some credit unions to rebrand or alter the focus of their messaging.

Although we have highlighted some general issues and weaknesses within the CU/CDFI provider landscape, our research also pinpointed areas of good practice too. Hence, for example, it is not universally the case that these providers are not able to offer near-real-time decision-making or an excellent digital customer experience; it is more accurate to say that these practices are not yet widespread. We highlight a few of these examples in **Figure 3**, below.

Figure 3: Credit union – technology case studies<sup>16, 17, 18</sup>

Clockwise CU	NHS CU	Leeds CU
<p>Clockwise CU serves the needs of more than 12,500 members across Leicester, Leicestershire and Rutland and has a current loan book of circa £4.6 million.</p> <p>The CU has been focusing on its digital offer, delivered principally through an internal development team of three. It has adopted an approach based on integration, and has delivered functionality including:</p> <ul style="list-style-type: none"> <li>• Open Banking integration, using True Layer.</li> <li>• App for members to manage accounts and make applications 24/7.</li> <li>• Streamlined workflow delivering the capability to offer instant/near-real time decisions on loans.</li> </ul>	<p>The NHS CU offers a wide range of financial services to more than 18,500 NHS employees and their family members, in Scotland and the North of England with a loan book of £15.1 million.</p> <p>The NHS CU became aware of changing member expectations and wanted to deliver a faster, more consistent way of engaging.</p> <p>It chose to partner with secure messaging app Nivo, to assist with onboarding and instant messaging style communications as well as Open Banking integration.</p> <p>Since implementation, turnaround times have improved and onboarding completion has moved from 35 per cent to 67 per cent.</p>	<p>Leeds Credit Union provides financial services to 37,000 members who live or work in Leeds, Wakefield, Harrogate and Craven as well as residents of certain housing associations and employers.</p> <p>The CU has a track record of embracing technology, for example, being able to offer payroll deduction schemes for many years and developing an automated school savings portal which replaced manual/paper based school savings club collections.</p> <p>The CU has also worked with other CUs/CDFIs, as part of the Affordable Loans Partnership, to develop a portal for affordable credit, as an alternative to higher-cost portals.</p> <p><a href="http://www.affordableloans.credit">www.affordableloans.credit</a></p>



## 4. Fintechs: What can they bring to the table?

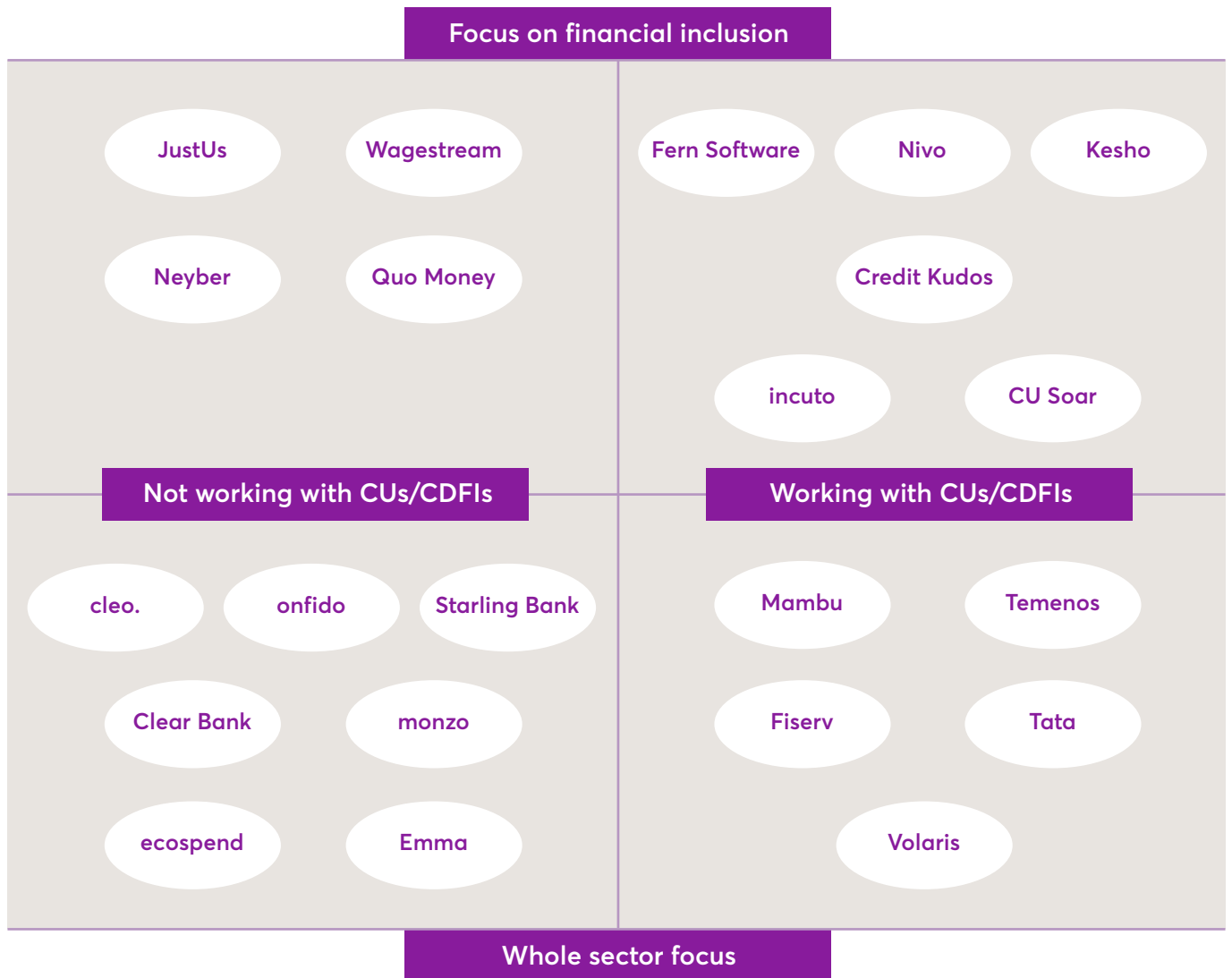
Fintech companies, using technologies to widen the access of consumers and businesses to new financial products and services, are working across many subsectors – changing our approach to banking, pensions, insurance, credit, cybersecurity and even regulation. These organisations are potentially able to offer several relevant technologies, which begin to address some of the issues and challenges identified above. We are already seeing novel approaches to assessment and credit scoring, payment profiling to suit unpredictable earning, and open banking integration.

### 4.1 The current UK social and community lending fintech landscape

Through our research into the sector, we undertook a brief overview of fintech suppliers that are already serving CU/CDFI customers; there is currently little in the way of a market for technology services to social and community lenders in the UK. We identified a handful of niche UK fintechs which are operating in this sector (largely startups and SMEs), as well as a few large global giants which are providing/offering banking platform services to UK CUs and CDFIs. In addition, we also highlighted a few UK fintechs who, while not operating directly in this space, are either offering fintech products which cater for those who would otherwise need to turn to high-cost, short-term credit, or which cater for a broad cross-section of society (i.e. potentially with a greater reach than, say, high street banks).

An overview of the landscape for technology suppliers working in UK financial inclusion is shown in **Figure 4**, below. We also include further detail on those companies currently working directly with CUs/CDFIs, in **Appendix 2**.

Figure 4: Fintech financial inclusion landscape<sup>19</sup>



## 4.2 What can fintechs offer?

Based on our research and discussions with companies in the fintech sector, we highlight six potential areas where these types of organisation could potentially partner effectively. This is summarised in **Figure 5**, below.

**Figure 5: Potentially relevant fintech capabilities**

	Relevant fintech capabilities	Potential applications
<b>Frictionless workflow</b>	Creation of products with more streamlined workflow (e.g. to allow faster decision-making)	Reducing manual data entry Automated forms, with decision algorithms Slicker on-boarding
<b>Customer/member acquisition and management</b>	Digital marketing, segmentation, brand building and search optimisation	Expanding advertising/marketing reach Raising awareness CRM functions to enhance consistent communications
<b>Scalable solutions</b>	Approaches which will lower unit cost of execution (e.g. shared platform or Blockchain/DLT-based systems)	Consolidated back-end New approaches to payment processing
<b>Digital experience (UI/UX)</b>	Overall customer experience (UI/UX). Offering greater immediacy, personalisation and customer experience	Simpler, cleaner, responsive design Enhanced communication/messaging services Behavioural analysis of drop-off points
<b>Integration</b>	Ability to integrate better into customers' own finances or to other third-party systems	Open banking integrations Payroll integrations Benefits systems integrations
<b>Analytics/AI/Data Science</b>	Data analytics and decision support Machine learning Chatbots / interfaces Voice/Face recognition and biometrics	Improved analytics for risk scoring / customer stratification Automated loan decisions (algorithms) Chatbots to assist customer journeys Machine learning to assist operational processes (e.g. early identification of problems) Automated verification and security

In terms of the potential direct applications of these six technology domains, there are plenty of opportunities for CUs/CDFIs.

### Frictionless workflow

Technology startups in general have long-observed the gains that can be made by ensuring that potential paying customers do not drop out along the journey. For CUs/CDFIs, the most important part of this is successful customer onboarding, taking a potential member/customer from the first click on the website to successful sign-ups to membership and access to credit. Fintech companies can help by optimising user-journeys (the typical user steps in a digital process), reducing the requirement for manual intervention and removing unnecessary friction (e.g. avoiding anything to do with paper or the postal system). Some providers are now using tools such as mobile instant messaging (see the Nivo case study above, for example) to maintain momentum.

### Customer/member acquisition and management

Another technology application which many fintechs (and technology startups in general) have solved is the use of online brand and marketing technologies to cost-effectively target new customers. Use of digital marketing tools (for example, using segmentation techniques to pinpoint customers based on their postcode, hobbies, lifestyle and even shopping habits) are common. Customer relationship management (CRM) technology also potentially provides more consistent ways of managing prospective and active members.

### Scalable solutions

Given the issues raised by CUs/CDFIs about critical mass and issues with the unit economics of low-value, short-term loans, a key objective would therefore be to reduce transaction costs to the lowest levels possible. Fintechs are developing a bunch of very specific technologies here, helping commercial customers with alternative transaction/payment processing technologies which lead to lower unit costs. We perceive there may be particular benefits where these technologies can be applied across multiple sub-scale organisations. This is already the case in the US, where there are established providers of back office services.

### Digital experience (UI/UX)

Another capability, related to the workflow above, is around creating excellent customer user interfaces and user experience in product development. This may include developing flexible product architecture, which can work across a variety of web and mobile platforms, and gamification techniques, to maintain a user's interest.

### Integration

A recurring criticism we heard about the existing systems that credit unions use was the lack of integration with other third-party systems. For example, this might include the capability to plug in a third-party ID verification or credit-scoring system, to integrate alternative open banking or payment processing systems or to be able to offer automated payments from employers' payroll. Although solutions do exist for the above examples, this is potentially an area where fintechs can contribute.

### Analytics/AI/Data science

Although CUs/CDFIs generate a wealth of potentially insightful customer data, fintech partners could potentially assist in turning this data into actionable insight. This might be through improved verification, decision-making analytics, or automated AI/Chatbots to improve customer journeys as a further enabler to improved workflow and user experience (above).

Many of the credit unions and CDFIs that we spoke with find it difficult to access the above capabilities on a consistent basis because, as small organisations, it is difficult to source the right skills. Even a relatively early-stage technology startup will typically have a development team, including a CTO, front and back-end developer specialists, business analyst, digital product lead and someone managing UI/UX. However, a single CU/CDFI is unlikely to have access to this set of skills.

We also researched the commercial short-term high-cost provider sector, to understand their own key points of differentiation. These can be summarised as:

- **Advertising and marketing**, to achieve high volumes of web traffic at relatively low cost. The leading commercial players are very astute at finessing their online advertising and marketing methods to achieve maximum returns. For example, this might include running hundreds of simultaneous marketing campaigns, with automated optimisation on the ones which generate the most return (lowest cost-per-click).
- **Low-cost back office processes**, involving a high degree of automation. To be successful and time-sensitive to customer loan applications, it is essential that there are the fewest possible points where human intervention is required. Examples of this might include fully automated checking of documentation (identity, address, bills) and algorithm-based decision-making.
- **Accurate credit assessment processes** (minimising write-offs etc). Commercial lenders may often set their own thresholds for acceptance based on their scoring of credit, affordability and other factors. This is a process which is evolving with techniques such as machine-learning now being adopted by some of the leading players and the use of non-standard data sources such as current account, social media and mobile phone data.<sup>20</sup>

At present, those outside the small immediate circle of providers who are already working with the sector in the UK do not appear well-sighted on these organisations and the potential opportunity to work with CUs/CDFIs. This is in contrast with the US, where there are several established players (such as some of those listed in **Appendix 2**) which have well-developed specialist offers for credit unions and where there has already been significant consolidation of some technology platform-based services, particularly around back-end services. Just focusing on credit unions alone, this is now a huge global market, of 90,000 credit unions, with assets of \$2,115 billion.<sup>21</sup> However, based on the conversations that we had with both fintechs and their potential customers, there was not the sense of an abundance of new entrants to this market – thus, in a similar vein to the challenge for social and community lenders around public awareness, there is also perhaps an issue within the sector of generating greater awareness with the fintech community.

# 5. Bridging the gap: Responding to different cultures and motivations

Bringing these two sectors together successfully will require overcoming cultural and strategic differences in these organisations. Building on the findings of our research, we highlight some of the potential key blocks to effective partnership working across the social and community lender and the fintech sector. We also summarise recommendations for the successful resolution of these blocks.

## 5.1 CU/CDFI blocks to participation

For credit unions and CDFIs, the most significant blocks appear to be organisational capacity, culture and partner selection. These themes are shown in **Figure 6**, and then expanded in more detail below.

**Figure 6: Blocks to fintech involvement and recommended resolutions**

	Block to participation	Suggested resolution
<b>Organisational capacity</b>	Unable to engage effectively as a consequence of lack of resource or client-side tech expertise	Focus on larger organisations as exemplars (possibly identify a cohort of fast followers) or allow consortia of smaller CUs or engage in upskilling/development programme alongside implementation
<b>Partner selection</b>	Difficult to evaluate which fintech to work with. Organisational stability is an issue	Assistance with due diligence (establish criteria or a framework of capable suppliers) NB need to square this with innovation and risk
<b>Culture and perceptions of past failures</b>	Risk averse and unwilling to jeopardise current operational processes. Nervousness about wasting time on initiatives which have not worked in the past	Clear about how it's going to be different this time. i) Not top down ii) Modular rather than big bang iii) Quick wins and agile approach

The most consistent theme running through our engagement with CUs/CDFIs was around **organisational capacity**. Many of the organisations in this sector are small, with few permanent staff and skills deficit in technology capability. This potentially has issues in terms of how well the sector might be able to engage with the fintech community. Specific issues include having the necessary resource for client-side engagement with fintech partners and being equipped with the technical knowledge to adequately define issues and requirements. This also links to a second issue, one of **partner selection**. CUs/CDFIs that we spoke with raised issues about their own competence to select an appropriately skilled fintech partner to work with. A particular fear around this issue was that this is very much startup territory and it was unclear whether the fintechs they were talking to today would still be around tomorrow.

### Recommendation one

Focus on the 20-30 larger CUs and the CDFIs as exemplar sites, but also raise awareness among the smaller organisations and make plans to facilitate a cohort of fast followers. Also consider the creation of joint ventures in order to concentrate resource and IP.

### Recommendation two

Assist the sector to engage effectively with fintechs. This might include conducting due-diligence or pre-screening of candidate fintechs, arranging partnering/speed-dating events to enable partnership formation, providing client-side tech support (e.g. through other more-established fintechs).

A further issue is rooted in **culture and perceptions of past failures**. This stems from the perception from some that we spoke with that past technology initiatives in this sector had failed and had led to time and money being wasted. These past failures had also perhaps driven a more risk-averse culture as a consequence. Criticisms of a previous related initiative (the 'Cornerstone' CU Expansion Programme) included claims that it was overly top-down, big-bang and not sufficiently user-designed and customer-focused. Also, that it had ultimately been narrowly focused around areas that were less central to key challenges faced. Our conversations chime with issues raised by the post-project review.<sup>22</sup>

### Recommendation three

Apply the lessons learned from previous initiatives from this sector. This might mean smaller, incremental initiatives, generating short-terms wins and greater CU-buy-in. Partners can also plan on the basis of an agile, iterative approach which aligns well to the development cycle typically adopted by fintechs.

## 5.2 Fintech blocks to participation

For fintechs, the most significant blocks appear to be customer readiness, sector knowledge and understanding the potential value that such a partnership might bring. These themes are shown in **Figure 7**, and then expanded in more detail below.

**Figure 7: Blocks to fintech involvement and recommended resolutions**

	Block to participation	Suggested resolution
<b>Readiness</b>	Customers are not ready or willing to embrace change	Case studies of current good practice (there are plenty of gems) and creating a vision/roadmap for the sector
<b>Sector knowledge</b>	The technical capabilities exist but the CU/CDFI landscape is alien	Briefing sessions and matchmaking within the fintech community to stimulate those with relevant transferable technologies
<b>Need for a CU/CDFI partner?</b>	Already has a proposition for finically excluded customers and does not see value in partnership	Articulate the win-win aspects of the challenge, e.g. opening up to a broader customer base (e.g. LA/NHS employers) and access to data and experience

There are also potential blocks to fintech participation in the programme. We heard from fintechs that they struggle to clearly communicate their product's goals and benefits to their CU/CDFI customer (i.e. generating better understanding and awareness of the benefits that their solution might bring). This is particularly true of CU/CDFI customers who do not currently have a strong tech offering and for those types of organisations there may be cultural resistance to technology change (particularly where it means changing the underlying business processes as well). Here, there appears to be a strong case for highlighting stories or examples of success to bridge this gap.

### Recommendation four

Identify and promote exemplar case studies from CUs/CDFIs and their tech partners which have successfully implemented new systems or ways of working. Use the potential of these successful cases to build a compelling vision of what the system could look like in three to five years' time.

A second barrier for fintechs is awareness of the sector. Many early-stage fintechs do not possess the sector knowledge to understand the specific needs and motivations of social and community lenders. However, this does not mean that these organisations have nothing to offer, since many of the requisite skills that we highlight in **Figure 5** above are common to suppliers currently working in related sectors. This means there is potentially a shortage of new fintech suppliers who might benefit from this opportunity.



### **Recommendation five**

Briefings and awareness sessions among the fintech community – suggest using fintech/startup communities to raise awareness and briefings/matchmaking events to assist new market entrants.

Finally, we note that there is a group of fintechs which are already offering their own products to financially excluded sections of society, independently of CUs/CDFIs. For some of these fintechs, it was unclear whether there is sufficient appetite or perceived benefit to them in partnering with CUs/CDFIs. For many, particularly larger organisations, the notion of partnering/cross-platforming was not on their strategic roadmap and was not likely to be a high priority.

### **Recommendation six**

Consider other ways of engaging with fintechs that may not currently have any appetite for working directly with the sector. This may include a clearer articulation of the potential partnering benefits for this group of fintechs or a specific focus on those fintechs which have a social purpose / close mission alignment. Alternatively, there may be ways that fintechs can be encouraged to work independently of a CU/CDFI partner, but with the same ultimate goals in mind.

# Appendix 1

## Personas

### Gaelle: The overstretched student

#### Attributes

Gaelle is studying at uni (Masters Degree in Fashion and Design at Bournemouth) and plans to set up her own label when she graduates in six months' time. She is a first generation scholar.

No savings but she does have a small overdraft on her current account and a maxed-out student loan (£32,000). She has no credit history (no credit card or previous personal loans).

Has taken on several part-time jobs (cafe and bar) to help fund her Masters but hours are not guaranteed and her income is unpredictable.

Recently she has struggled to pay her rent because of other unexpected outgoings (she was burgled and her laptop was stolen – it wasn't insured).

#### What problems does Gaelle have that fintechs/ CU/CDFIs can solve?

Credit history limited which affects her ability to take out a credit card or personal loan.

Doesn't really understand credit scoring and vaguely worried that she may be penalised if she checks it.

She's not connected to anyone else who could help her out.

#### Goals - Gaelle would like to be able to:

Access affordable credit quickly (on a just-in-time basis).

Find flexible payment terms, if problems crop up.

Build a credit history and know where she stands with this.

Access services via a simple app on her iPhone.

Receive advice on most cost-effective options.

#### Quote

*"Just find me an app that's quick, simple and doesn't try to rip me off."*

#### Triggers

Financial shock (if sudden large items are required).

No awareness of affordable credit lines, so borrowing more likely to result in indebtedness.

## Cassie: Struggling single mum

### Attributes

Cassie is a single mum living in a small flat with her three-year-old daughter, Marley. She claims benefits but also juggles her own childcare with a few hours at local nursery, where she works as a childminder during term-times.

She is very careful with money and doesn't trust banks or lenders after one of her friends ended up with debts that she couldn't repay. She uses

the Very and Next catalogues to buy clothes and essentials for herself and her daughter. She is currently in arrears with some of her utilities providers.

She thinks about her outgoings in terms of 'weekly payments' and budgets on the basis of what she has to spend each week.

### What problems does Cassie have that fintechs/ CU/CDFIs can solve?

Wants transparent low-cost credit without any pressure or complicated APR jargon.

Flexibility so that she can pay more or less without penalties.

She tends to think about her problems in terms of what she wants to buy and how much she can afford each week rather than how much she wants to borrow.

### Goals – Cassie would like to be able to:

Get more for her weekly budget, including larger items for her home.

Have peace of mind that things won't go downhill during the periods when there's no work.

Be treated without pressure or complicated financial terminology.

Rely less on her default options like store cards.

### Quote

*"I need a trusted and affordable way of buying the items I need."*

### Triggers

Unstable employment, unreliable income.

## Harry: Just back into work

### Attributes

Harry left school without any qualifications. He is now back into part-time employment as a delivery driver after a spell of unemployment and depression. He has a partner who also has a part-time cleaning job and he has two young children, the oldest has just started school. He earns around £15k.

Harry would see himself in the 'financially struggling' category. He took out various payday loans before they were properly regulated and then high interest loans to consolidate his debt. It was easy to do this on his mobile phone and

less embarrassing than talking to a person about borrowing money. However, he subsequently defaulted on his payments when he became unemployed and his claim for Universal Credit took a month to come through. He closed his bank account when the charges rocketed. He now doesn't trust banks or lenders.

He has a credit history – but his rating is poor as a consequence of past performance. He was recently turned down for a high-street personal loan but was offered one from an online provider, but with a rate that he thought was unreasonable.

### What problems does Harry have that fintechs/ CU/CDFIs can solve?

Turned down for conventional credit – perhaps seen as too risky.

Low income and, with no savings, has a week-by-week view in relation to making ends meet.

Low awareness of alternatives and doesn't really click with concepts of interest rates / APRs.

### Goals – Harry would like to be able to:

Not get turned down, because of his past circumstances.

Be better informed about options / choices and have banking options which didn't start imposing large fees.

Start thinking about larger things like a new sofa or TV or taking a holiday later in the year.

Be better prepared if he does lose his job again in the future.

Know who to trust when they say this is 'a good deal'.

### Quote

*"I don't want to be spending all my wages paying off interest."*

### Triggers

Potential mental health issues, related to stress around finances.

Financial shock (no savings, so not well insulated against shock).

## Joan: Retired and vulnerable

### Attributes

Joan is 78 and has been retired for over 15 years. She is a widower, and lives alone in a small bungalow in the centre of her village. She receives a small pension and just about manages on her income, although she struggles more in the winter when her outgoings are higher.

She has never been a confident user of the internet and her husband used to manage the bills. She used to use the Post Office in the village for her savings, until it closed down and she now

takes a trip to the town to use the bank when she needs to. She has been visited a few times by a doorstep lender who gave her a glossy brochure and was very charming.

More recently she is beginning to get a bit forgetful, going to the shops and forgetting what she went to buy. Her two children live in the city, about an hour away, and visit her every month or two.

### What problems does Joan have that fintechs/CU/CDFIs can solve?

Doesn't really understand the internet and feels a bit left behind.

Access to services and advice is a problem for Joan and she doesn't want to impose on her family.

She wants to remain independent in her own home but is worried about increasing costs.

### Goals – Joan would like to be able to:

Know that her savings and income is safe and that she can cope.

Understand what her options are instead of the Post Office.

Be able to have the occasional treat for herself or her grandchildren once in a while.

### Quote

*"Everyone seems to do everything on the World Wide Web these days."*

### Triggers

Vulnerability as a consequence of deteriorating health.

Unable to navigate the system to find effective alternatives.

# Appendix 2

## Fintech providers: Companies providing services to UK CUs/ CDFIs and those with a focus on fairer finance/inclusion

### Credit Kudos

Credit Kudos is an FCA-authorized credit bureau and Account Information Service Provider (AISP) startup that uses financial behaviour to measure creditworthiness.

### CU Soar

CU Soar (recently rebranded to Soar) includes a mobile application and back-end content management system (CMS), which can be integrated with legacy back-end banking systems that credit unions use.

### Fern Software

Fern Software provides systems with a focus on inclusive financial institutions. It delivers to 300+ organisations in over 30 countries. Its HQ is in Northern Ireland.

### Fiserv

Fiserv is a US-based financial services technology solutions provider, with a specific offering for CUs. 12,000 clients worldwide, including one third of US credit unions. Revenues of >\$5 billion. A presence in the UK and part of the CU Expansion Programme initiative.

### incuto

incuto is a hosted banking technology platform startup, facilitating social and community lenders through back-office efficiency, improved access to information and access to payment networks.

### JustUs

JustUs focuses on consumer mortgages and loans, offering an inclusive approach.

### Kesho

Kesho provides the core system used by many UK-based credit unions (account system, ledgers' credit management, online banking, messaging).

### Mambu

Mambu is a US-based banking platform and technology company, serving nine million customers in 55 countries with a portfolio valued at \$4.5 billion.

### Neyber

Neyber aims to provide fairer finance and improve financial wellbeing for its customers through employer-based savings and loans products. A key business strand is loans via employer payroll deductions, with over 350 employers, 1.3 million customers and a loan book of £130 million.

### Nivo

Nivo is a provider of instant message based services. Current offer includes onboarding (identity verification, open banking, E-Signing and automation) to offer improved customer service/sign-up experience.

### Quo Money

Quo Money provides an app-based service that aims to promote money management skills among vulnerable consumers. It uses Open Banking to generate a personalised financial plan and prompts the consumer to adhere to it.

### Tata

Tata provides the TCS BaNCS solution, an integrated platform providing banking, cards and payment functions. Working with UK based CUs.

### Temenos

Temenos is a Swiss-based company providing banking platforms in over 40 countries worldwide. It provides inclusive banking, delivered on-site or via the cloud as a subscription-based, Software-as-a-Service (SaaS) model.

### Volaris

Volaris Group holds over 50 companies working in various verticals. This includes Wellington IT, based in Ireland, offering core financial systems, online and member services as well as IT managed services.

### Wagestream

Wagestream's offer allows employees to access a percentage of their wages as they are earned, stream their salary directly into a savings account and get financial education in real-time. Other players in this space include Karma and Salary Finance.

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