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EVALUATION OF THE DWP GROWTH FUND

REVISED FINAL REPORT

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The views expressed in this report are the authors' own and do not necessarily reflect those of HM Treasury or DWP

Contents

Executive summary 5

1 Introduction 8

1.1 Aims of the evaluation 8
1.2 Research methods 9
1.3 This report 9

2 Profile of Growth Fund applicants 11

2.1 Socio-demographic characteristics of Growth Fund applicants 11
2.2 Employment, income and standard of living 11
2.3 Applicants' views about their financial situation 12
2.4 Differences between successful and unsuccessful Growth Fund applicants 13

3 Impacts of the Growth Fund on borrowers' credit use and financial situation 15

3.1 Do Growth Fund borrowers use other sources of borrowing as well as the Growth Fund? 15
3.2 Amounts borrowed from the Growth Fund and other sources of borrowing 17
3.3 Had Growth Fund borrowers changed their borrowing behaviour? 18
3.4 The financial benefits of borrowing from the Growth Fund 20
3.5 The material benefits of borrowing from the Growth Fund 22

4 Other impacts of the Growth Fund on borrowers 24

4.1 Banking 24
4.2 Saving 25
4.3 Financial capability 28

5 Unsuccessful Growth Fund applicants 30

5.1 Why were Growth Fund loan applications turned down? 30
5.2 Did unsuccessful applicants know why their loan application was refused? 31
5.3 Were unsuccessful applicants referred to an advice agency? 31
5.4 Actions taken by unsuccessful applicants when turned down 32
5.5 Were unsuccessful applicants likely to re-apply to the same Growth Fund lender? 33
5.6 Growth Fund lenders' views of un-served or under-served groups 34

6 Impact of the Growth Fund on third sector lenders 35

6.1 Were third sector lenders more business-like as a result of the Growth Fund? 35
6.2 Volumes of lending 39

6.3 Customer profile 40
6.4 Would Growth Fund lenders continue to lend to financially excluded people post-2011? 40
6.5 Were Growth Fund lenders dependent on grant funding? 41
6.6 Future funding 42
6.7 Working with Growth Fund lenders: the views of other community organisations .. 44

7 The costs and benefits of the Growth Fund 46

7.1 Costs 46
7.2 Benefits 50
7.3 Conclusions 55
7.4 Estimating a commercial rate of return 57

8 Summary and conclusions 60

8.1 Did the Growth Fund increase access to affordable credit? 60
8.2 Growth Fund borrowers 61
8.3 Growth Fund lenders 63
8.4 The costs and benefits of the Growth Fund 67

Executive summary

The objective of the DWP Growth Fund was to raise levels of access to affordable credit by building the capacity of third sector lenders to serve financially excluded households. In doing so, the Growth Fund aimed to disrupt the role of high cost credit in the lives of borrowers.

Access to affordable credit in deprived communities

DWP management information reported that:

- 317,798 Growth Fund loans were made in deprived communities from July 2006 up to the end of September 2010, with a total value of over £137 million
- An additional 12,090 loans were made in October 2010
- An average of 30 per cent of all successful loan applicants reported having a recent record of borrowing from a high cost lender, and
- 98 per cent of successful loan applicants reported having borrowed from high cost lenders at some point in their lives.

DWP reported that Growth Fund loans and associated financial services are available to financially excluded individuals from about 150 lenders (the number has fluctuated slightly as credit unions merged or new lenders joined the project) serving about 400 towns, cities, and several rural locations across Great Britain. This level of service to financially excluded communities did not exist prior to 2006.

Repeat use of Growth Fund lenders was common. Survey data found that 68 per cent of Growth Fund borrowers had applied for loans on two or more occasions, usually successfully. These subsequent loans were not necessarily funded by the Growth Fund, and the telephone survey of lenders found that non-Growth Fund loans were generally offered at lower rates of interest, typically around 12 per cent APR.

Analysis of the survey data indicates that 79 per cent of Growth Fund borrowers were in the two lowest income quintiles. One in five Growth Fund applicants (20 per cent) did

not have a current or basic bank account. Growth Fund lenders were also primarily serving a completely new market: only four per cent of applicants in the survey said they were already a credit union member or CDFI customer at the time of their Growth Fund loan application.

Impacts on Growth Fund borrowers

The impact assessment of the Growth Fund carried out for this evaluation (based on analysis of Growth Fund borrowers and a matched comparison group living in deprived non-Growth Fund areas) estimates total interest savings per Growth Fund borrower of between £377 and £425 over the lifetime of their current credit obligations.

In terms of actual credit use among Growth Fund borrowers, the survey data found that 50 per cent of Growth Fund borrowers had some other form of borrowing as well as the Growth Fund, although some of the most common types of borrowing they used did not incur interest charges. 32 per cent of Growth Fund borrowers considered that they had borrowed less from any other source since first taking out a loan with a Growth Fund lender. Almost all of these borrowers (87 per cent) attributed this change in behaviour directly to their contact with a Growth Fund lender. There was evidence that the Growth Fund had disrupted the role of high-cost credit in borrowers' lives, with 12 per cent of all borrowers reporting that they had used home credit less since first contacting a Growth Fund lender.

Contact with a Growth Fund lender had resulted in additional benefits to applicants, over and above the main objectives of the scheme. 13 per cent of banked Growth Fund applicants had a bank account as a result of their contact with a Growth Fund lender. 29 per cent of applicants now had savings in a savings account, whereas previously they had none. There was evidence of the effective use of 'soft compulsion' by lenders to encourage saving among low-income borrowers at the point of lending.

Among successful applicants, 39 per cent felt their money management skills were better since they had started using a Growth Fund lender. Similar proportions said they felt more in control of their finances (41 per cent); more financially secure (39 per cent) and less worried about money generally (37 per cent).

Impacts on Growth Fund lenders

Growth Fund lenders who took part in the telephone survey had considerably increased in size and in terms of volumes of personal lending (Growth Fund and non-Growth Fund) between 2006 and 2009. Eight in ten Growth Fund lenders reported that their organisation had improved its working practices as a result of the Growth Fund and now operated in a more business-like way.

Higher interest rates than the 26.8 per cent charged by most Growth Fund lenders would be needed to put current Growth Fund lending on a more stable commercial platform, however. It is estimated that, based on average operating costs since 2006, an APR of 71.2 per cent would be required to cover operational costs and financial risks associated with Growth Fund lending. Based on 2010 average operating costs, the required APR is estimated to be 39.6 per cent to break even at a cost of £60 per loan, and 48.1 per cent to break even at a cost of £75 per loan.

The costs and benefits of the Growth Fund

The cost of the administering the scheme totalled £40.8m, with the additional social cost of lending estimated at £14.3m. The scheme also displaced the profits of commercial lenders (including higher-cost lenders and other credit providers). These displaced profits are estimated to total a maximum of between £21.3m to £30.5m.

In terms of benefits, the Growth Fund was found to have reduced the interest paid by borrowers on their lending by reducing the interest rate paid and by shortening the period over which borrowers repaid their debts. Based on the 317,798 loans made to the end of September 2010, total interest savings to financially excluded individuals in deprived communities are estimated between £119.1m and £135.1m, of which between £41.3 and £48.9m represent interest rate savings.

Additionally, as the Growth Fund was mainly accessed by those in lower income groups, there was a further distributional effect of between £89.9m and £101.3m based on total interest savings.

1 Introduction

The objective of the DWP Growth Fund was to raise levels of access to affordable credit by building the capacity of third sector lenders to serve financially excluded households. In doing so, the Growth Fund aimed to disrupt the role of high cost credit in the lives of borrowers.

The Growth Fund had three elements. First, it provided loan capital to third sector lenders, mainly credit unions and community finance development institutions (CDFIs) to lend to financially excluded households. Secondly, it provided revenue to Growth Fund lenders to support the delivery of loans, for example to help cover administrative and staff costs. Thirdly, there was funding to develop the capacity of third sector lenders.

DWP management information records that 317,798 Growth Fund loans were made from July 2006 up to the end of September 2010, with a total value of over £137 million. An additional 12,090 loans were made in October 2010.

1.1 Aims of the evaluation

HM Treasury commissioned The Personal Finance Research Centre (University of Bristol) and ECORYS to evaluate the DWP Growth Fund. The evaluation was undertaken between December 2009 and August 2010. It aimed to establish the following impacts of the Growth Fund on Growth Fund borrowers and lenders:

Group	Impact Measures
Borrowers	Propensity to use high-cost or illegal credit
	Access to, and use of, appropriate financial services
	Savings on interest payments
Growth Fund Lenders	Overall customer profile
	Lending practices
	Levels of business and capacity
	Use of other streams of funding

It included an appraisal of the costs and benefits of the Growth Fund, and an estimation of a risk-based rate of interest associated with Growth Fund loans.

1.2 Research methods

The evaluation comprised qualitative and quantitative research methods:

- In-depth qualitative case studies with eight Growth Fund lenders, including depth interviews with staff, successful and unsuccessful Growth Fund applicants, and other organisations that deliver services to financially excluded people.
- Quantitative surveys of individuals:
    - 504 successful Growth Fund applicants
    - 328 unsuccessful Growth Fund applicants
    - A comparison group of 520 individuals drawn from 16 local authority areas with very little or no Growth Fund coverage but with potential demand for lower cost credit.
- A telephone survey of 82 Growth Fund lenders and a group of 25 non-Growth Fund lenders.

Full details of these research methods are provided in Appendix 1.

Analysis of Growth Fund management information was also carried out, comprising a random sample of 50% of all Growth Fund loan applications from the start of the scheme in July 2006 to the end of December 2009.

1.3 This report

Chapters 2-5 include descriptive analysis of the quantitative surveys of successful and unsuccessful Growth Fund applicants and qualitative findings from the eight case studies. Chapter 2 provides a profile of Growth Fund applicants. Chapter 3 examines the impacts of the Growth Fund on borrowers' credit use and financial situation, as reported by borrowers themselves. Chapter 4 outlines the additional self-reported positive impacts of the Growth Fund on borrowers. The tables for Chapters 2, 3 and 4 are provided in Appendix 3. These tables include the comparison group where appropriate, but these data are not discussed in the body of the report.

Chapter 5 goes on to explore the experience and views of unsuccessful Growth Fund applicants. In Chapter 6, we outline the impact of the Growth Fund on third sector lenders, drawing on the telephone survey of lenders and the qualitative case studies.

The data from the comparison group survey were collected specifically to carry out the impact assessment that forms the basis of the analysis of costs and benefits in Chapter 7. Unlike the analysis reported in earlier chapters which describes the self-reported views and experiences of Growth Fund borrowers, the impact assessment establishes the counterfactual: in other words, in the absence of the Growth Fund, what could we reasonably expect borrowers to have done? In particular, Chapter 7 examines the savings on interest payments that occurred as a result of the Growth Fund. Full details of the impact assessment analysis are provided in Appendix 2.

2 Profile of Growth Fund applicants

The DWP Growth Fund was targeted at low-income and financially excluded households living in deprived areas of Britain. This chapter draws on the survey data to provide a profile of Growth Fund applicants (both successful and unsuccessful applicants). It then goes on to explore the main differences between successful and unsuccessful applicants in terms of key socio-demographic characteristics. Full breakdowns of the statistics presented in this chapter are available in Table A2.1 in Appendix 3. Credit use is examined in Chapter 3.

2.1 Socio-demographic characteristics of Growth Fund applicants

The Growth Fund management information indicates that Growth Fund applicants are typically women, and people aged between 25 and 44. The survey data broadly reflect this profile: the majority of Growth Fund applicants surveyed were women (71 per cent) and six in ten respondents (62 per cent) were under 40 years old.

61 per cent of applicants were families with dependent children, with twice as many lone parents as couples with children (40 per cent compared with 21 per cent respectively). Most families included one or two children, but a significant minority were larger families with three or more children (equivalent to 15 per cent of all applicants). Single adult households made up 21 per cent of all applicants surveyed. The great majority of applicants described themselves as White (93 per cent).

Nine in ten Growth Fund applicants rented their homes, in most cases from a housing association or local authority (71 per cent). Very few (four per cent) owned their home.

2.2 Employment, income and standard of living

More than three quarters of Growth Fund applicants (77 per cent) were not in paid employment. The majority of them fell into one of three groups:

- Looking after the home/caring for family (32 per cent of all applicants)

- Unemployed and looking for work (20 per cent)
- Unable to work because of ill-health or disability (18 per cent).

At a household level, seven in ten applicants (72 per cent) lived in a household with no earners. This was reflected in the sources and levels of household income that they reported:

- Nine in ten applicants (92 per cent) reported that their household received some benefits or tax credits.
- Half of applicants (52 per cent) received income-replacement benefits (Income Support, Jobseekers' Allowance or Incapacity Benefit) plus some other benefits or tax credits (such as Disability Living Allowance).
- Two-thirds of applicants (67 per cent) reported net (banded) household incomes less than £300 per week. A significant minority (15 per cent of applicants) had household incomes less than £100 per week.

To gauge standard of living, applicants were also asked whether they had gone without a range of items because of a lack of money in the past 12 months.[1] Eight in ten applicants (82 per cent) said they had gone without at least one of the 12 items listed; half (52 per cent) had gone without four or more of the 12 items. The most common things that applicants had gone without were:

- A week's annual holiday away from home
- Going out or socialising
- Putting away £10 each month for a rainy day
- Household contents insurance.

2.3 Applicants' views about their financial situation

Applicants' were asked a range of questions to establish how well they were able to make ends meet. Three-quarters of applicants (74 per cent) said they were keeping up with their household bills and credit commitments, but it was a struggle at least some of

[1] A similar list of items has been used on the Family Resources Survey to assess material deprivation.

the time. And two-thirds of applicants (65 per cent) said they ran out of money before the end of the week or month at least sometimes.

Four in ten applicants (38 per cent) had been unable to pay at least one household bill (excluding consumer credit) at the final reminder in the last 12 months due to a lack of money. Fuel and water bills were the payments most often missed.

2.4 Differences between successful and unsuccessful Growth Fund applicants

As we go on to discuss in section 6.1.1, Growth Fund lenders used a combination of methods to reach a loan decision, including information collected on application forms, interviews, and credit checks. Factors such as the purpose of the loan and applicants' honesty in providing the required information were taken into account when considering a loan application. Lenders reported that insufficient disposable income was by far the most common reason for them to turn down a Growth Fund loan application (section 5.1).

Logistic regression analysis was used to explore the statistical probability that an individual applicant would be successful in their Growth Fund loan application (Table A2.2, Appendix 3). Growth Fund applicants' money management was a significant factor in terms of the probability of making a successful Growth Fund application, all other things being equal. So, applicants who reported that they had borrowed more than they could afford had a particularly low probability of success. Additional analysis to predict the chances of Growth Fund applicants having other types of borrowing indicated that the odds of having other borrowing was 40 per cent higher for unsuccessful applicants than successful applicants (Table A3.2).

Credit history was another strong independent predictor of a successful outcome, all other things being equal. As a result, having had a credit application turned down or a bad credit rating in the last five years reduced the chances of a successful Growth Fund loan application (Table A2.2).

The analysis also found that economically inactive applicants were more likely to be successful than those unemployed (and equally likely as those in employment), and this may reflect an expectation that loans will be repaid from benefits. Total household income (as distinct from disposable income) was not found to be a statistically significant

explanatory factor in the success of Growth Fund applications (Table A2.2). Average monthly household incomes were not greatly different across the two groups of applicants (£840 per month for successful applicants compared with £740 for unsuccessful applicants), and were correlated with employment status.

Finally, applicants' ethnicity was found to be a statistically significant predictor of whether or not a Growth Fund application would be successful, with White applicants having a greater probability of success than non-White applicants (Table A2.2). DWP management information reported that, at the time of evaluation, 69,204 loans had been made to people who described themselves as other than White British, which represented 21 per cent of Growth Fund loans overall.

3 Impacts of the Growth Fund on borrowers' credit use and financial situation

The 'hard' impacts of the Growth Fund – potential savings on interest payments for borrowers and the impact of the Growth Fund on total borrowing – are covered in Chapter 7.

This chapter starts by looking at whether Growth Fund borrowers used other sources of borrowing as well as the Growth Fund, before going on to examine levels of total current borrowing. Later sections look at some of the 'soft' impacts of the Growth Fund: whether borrowers had changed their borrowing behaviour as a result of the Growth Fund and the perceived financial and material benefits of borrowing from the Growth Fund. The chapter finishes by examining whether Growth Fund borrowers were aware of the costs of borrowing.

3.1 Do Growth Fund borrowers use other sources of borrowing as well as the Growth Fund?

The survey data indicates that a considerable proportion of Growth Fund borrowers used other forms of borrowing as well as the Growth Fund. At the time of the survey interview, half of Growth Fund borrowers (50 per cent) had some other form of borrowing (usually one or two different types at most). The types of borrowing most often mentioned were:

- Social Fund (mentioned by 15 per cent of Growth Fund borrowers)
- Hire purchase (including rental purchase) (14 per cent)
- Goods bought in instalments from a mail order catalogue (14 per cent)
- Loans from friends or family members where no interest was charged (11 per cent)
- Home credit loans (nine per cent) (Table A3.1).

The commercial credit options used by Growth Fund borrowers were those typically associated with high APRs (home credit) or with high mark-up on goods and additional

charges which may add to the total cost of borrowing (mail order and hire purchase). The other main sources of borrowing for Growth Fund borrowers were non-interest bearing (i.e. Social Fund loans and loans from friends and family). Some of the common sources of borrowing mentioned by survey respondents are described in Box 1.

Use of other sources of borrowing was much less common. Fewer than one in ten Growth Fund borrowers (eight per cent) were overdrawn at the time of the survey. As we see from Table A4.1, rather more Growth Fund borrowers (42 per cent) had a basic bank account which does not provide access to an overdraft facility, than had a current account (39 per cent), Four per cent of borrowers had an outstanding balance on a credit or store card. Only two Growth Fund borrowers in the survey (less than one per cent) admitted to having a loan from an unlicensed lender (Table A3.1).

Box 1: Sources of borrowing used by people on low incomes

Home credit companies (such as Provident Financial) offer small short-term cash loans with typical APRs ranging from 100% to 400%, although there are no further charges for missed payments. Home credit repayments are collected from the borrower's home.

Hire purchase allows people to buy goods such as white goods, furniture or cars on credit over a period of time. In contrast to hire purchase, goods bought from a rental purchase shop (such as BrightHouse) can be repossessed if payments are missed at any time until the total price of the goods has been paid. The APR for goods bought from a rental purchase shop is generally 29.9%, although the effective APR rises once insurance and price mark-ups on the goods are taken into account.

Agency mail order companies advertise that goods on credit are sold interest-free if repaid over 20 to 40 weeks, and at an APR of 28.8% if repaid over a longer period. Price-mark-ups add considerably to the cost, and can lead to effective APRs of up to 100%.

Social Fund Budgeting Loans aim to help eligible people on means-tested benefits with essential lump-sum expenses such as white goods or furniture. Budgeting Loans have to be repaid but they are interest-free. Social Fund Crisis Loans provide help to people who need money quickly because of expenses in an emergency or disaster. Like Budgeting Loans, they have to be repaid but are interest-free. Both Budgeting and Crisis Loans are provided on a discretionary basis.

3.1.1 Had Growth Fund borrowers taken out any other type of loan since receiving a Growth Fund loan?

Growth Fund borrowers who were repaying any type of loan (including loans from friends and family, Social Fund loans and loans from unlicensed lenders) were asked if they had taken out the loan before or after their Growth Fund loan.

Just over one in ten Growth Fund borrowers (14 per cent) said they had taken out a loan *after* their Growth Fund loan (Table A3.3). In almost all cases this was either a loan from the Social Fund or a home credit loan. A similar proportion of borrowers (11 per cent) were repaying a loan that they had taken out *before* their Growth Fund loan (Table A3.4). Again, this tended to be either a Social Fund or home credit loan.

3.2 Amounts borrowed from the Growth Fund and other sources of borrowing

The average (mean) loan amount originally borrowed from the Growth Fund by the successful applicants in the survey was £478. 78 per cent of borrowers in the survey were still repaying this Growth Fund loan. The remaining 22 per cent had already repaid their loan.

The survey data were used to calculate the total amount of borrowing that Growth Fund applicants currently had. This included the original amount borrowed in any loans taken out that were not yet paid off (including Growth Fund loans, loans from the Social Fund, loans from a friend or family member, and loans from an illegal lender), any amounts outstanding on credit or store cards, amounts overdrawn on a bank account, value of goods bought on hire purchase, and amounts owed on goods bought on instalment from a mail order catalogue.

The average (mean) amount of total current borrowing for Growth Fund borrowers (including outstanding Growth Fund loans) was £826. When current Growth Fund loans were excluded, this figure dropped to £402; the equivalent figure for unsuccessful Growth Fund applicants was £555. In other words, the Growth Fund accounted for 51 per cent of total current borrowing among successful applicants' who had any borrowing at the time of the interview.

Looking only at commercial borrowing (including illegal lending), the average total amount borrowed among successful applicants was £281. Among unsuccessful applicants it was much higher, at £430 (Table A3.5).

As we go on to discuss in Chapter 7, the assessment of costs and benefits carried out by ECORYS (comparing a matched group of Growth Fund borrowers and individuals from the comparison group) indicated that the Growth Fund had no impact (positive or negative) on the total amount borrowed by individuals. One implication of this finding is

that borrowing from the Growth Fund had not served to increase borrowers' overall debt burden.

3.2.1 Awareness of the costs of borrowing

In the UK, lenders have a statutory obligation to provide information about the cost of borrowing to their customers. The majority of Growth Fund borrowers surveyed (76 per cent) were either able to report the APR of their Growth Fund loan, the total amount that they had to repay on the loan (including the amount borrowed and any interested charged), or both. The remainder (24 per cent) could not say what the APR was or how much in total they had to repay (Table A3.6).

Levels of awareness were remarkably similar among the small proportion of Growth Fund borrowers who were repaying a loan from a high-cost lender (i.e. home credit loan, payday loan, loan from a pawnbroker or from an unlicensed lender). So again, while most could report the APR or the total amount they had to repay (or both), around a quarter could not say what the APR or the total amount they had to repay was.

3.3 Had Growth Fund borrowers changed their borrowing behaviour?

Growth Fund borrowers were asked if they had changed their borrowing behaviour since first starting to borrow from a Growth Fund lender. A third (32 per cent) considered that they had borrowed less from any other source (including friends and family and the Social Fund) since first taking out a loan with a Growth Fund lender (Table A3.7). Almost all of these borrowers (87 per cent) attributed this change in behaviour to their contact with a Growth Fund lender (Table A3.8). Less than one in ten Growth Fund borrowers (seven per cent) said they had borrowed more from any other source (Table A3.9). By way of comparison, only nine per cent of unsuccessful applicants said they had borrowed less since contacting a Growth Fund lender (Table A3.7), and more than twice as many (19 per cent) said they had borrowed more (Table A3.9).

As noted in section 3.1, home credit loans, loans from friends and family and Social Fund loans were the types of cash loans that applicants were most often repaying. There was evidence from the survey data that the Growth Fund had disrupted the role of high-cost credit in borrowers' lives. Around one in ten of all borrowers (12 per cent) said

they had used home credit less since first contacting a Growth Fund lender. A smaller proportion (nine per cent) said their home credit use had remained about the same. Only a handful of Growth Fund borrowers (one per cent) said they had used home credit more since coming into contact with a Growth Fund lender (Table A3.10).

There were similar changes in relation to Social Fund use and borrowing from friends and family and. 13 per cent of borrowers reported using the Social Fund less since using a Growth Fund lender, although rather more than this (16 per cent) said their Social Fund use had remained unchanged. Two per cent of borrowers said they had used the Social Fund more since coming into contact with a Growth Fund lender (Table A3.11).

Nine per cent of borrowers reported borrowing less from their family and friends since coming into contact with a Growth Fund lender. About twice as many (19 per cent) said they continued to borrow from friends and family much as before; one per cent said they borrowed more (Table A3.12).

For each of these three types of borrowing, unsuccessful Growth Fund applicants were more likely to say their use had increased or stayed the same, and correspondingly less likely to report a reduction in borrowing.

3.3.1 Future borrowing from Growth Fund lenders

The survey data indicated that the great majority of Growth Fund applicants were completely new to the Growth Fund lender they used. Only a small proportion (four per cent) comprised existing members or customers of that particular credit union or community development finance institution (CDFI) (Table A3.13).

The survey data showed that, once someone had successfully applied for a loan from a Growth Fund lender, they were very likely to apply again. Seven in ten (68 per cent) of Growth Fund borrowers in the survey had applied two or more times (Table A3.14). In most instances, these subsequent applications were also successful although the loans issued may not necessarily have been funded by the Growth Fund. The telephone survey of Growth Fund lenders indicated that the interest rates they offered for non-Growth Fund loans were typically between one and one and a half per cent per month (or around 12 per cent APR).

When asked directly, the majority of Growth Fund borrowers (95 per cent) said they would apply for a loan from the same lender again (Table A3.15). Almost two-thirds (63 per cent) said that a credit union or CDFI would be their preferred means of raising £500 (Table A3.16).

3.4 The financial benefits of borrowing from the Growth Fund

For the financially excluded people targeted by the Growth Fund, the total cost of a cash loan from a Growth Fund lender is significantly cheaper than the commercial equivalents (such as home credit, payday lenders, pawnbrokers or illegal lenders). The lower rate of interest offered by Growth Fund lenders was by far the most common reason why applicants had contacted the lender in the first place, mentioned by 65 per cent of successful applicants (Table A3.17). This may suggest that some people on low incomes are aware of the total cost of different sources of credit, and consider this alongside other important factors such as the weekly repayment amount.

The survey data indicated that the average value of a Growth Fund loan was £478 and Growth Fund management information indicates that the majority of loans (93 per cent) were provided at an APR of 28% or less. By way of example, a £478 loan from a Growth Fund credit union, repaid at £10.52 per week for 52 weeks at an APR of 26.8% results in a total charge for credit of £59.71. A £478 home-collected loan from a home credit company, repaid over 52 weeks at £16.73 per week at an APR of 272.2% results in a total charge for credit of £391.96.[2]

Most of the successful applicants who were interviewed in depth reported having borrowed from high-cost lenders at some time in the past, such as home credit companies, finance companies or mail order catalogues (which have high mark-ups). They generally considered the cost of borrowing from the Growth Fund to be lower in terms of interest and the total cost of the loan.

> *You're only paying back what you borrowed and a little tiny bit; where with [home credit company] you'd probably pay back double that.*

> *Comparing this now with like [home credit company] and that, which is about £200 [interest]... I've definitely finished with them. They're robbing the poor.*

---

[2] Comparison conducted using www.lenderscompared.org.uk

Additionally, the survey indicated that not all Growth Fund borrowers would have taken out a cash loan from a high-cost lender, if they had not been able to borrow from the Growth Fund. We estimate that one-fifth of Growth Fund borrowers (20 per cent) may have taken out a home credit loan, a payday lender, a pawnbroker or an illegal lender. This is based on whether or not borrowers had tried to borrow from any of these sources prior to applying to the Growth Fund; whether they were a current user of any of these forms of credit; or whether they reported that they were likely to have considered using any of these lenders if their Growth Fund application had been turned down.

As we go on to discuss in Chapter 7, the impact assessment of the Growth Fund carried out for this evaluation (based on analysis of Growth Fund borrowers and a matched comparison group living in deprived non-Growth Fund areas) estimates total interest savings per Growth Fund borrower of between £377 and £425 over the lifetime of their current credit obligations. Based on the 318,000 Growth Fund loans made to the end of September 2010, this means that an extra £119.1million and £135.1million was available to individuals and households in the local communities served by the Growth Fund in the form of total interest savings.

3.4.1 Repaying Growth Fund loans

As well as the overall cost of borrowing, the Growth Fund might also offer financial benefits to borrowers in terms of the affordability of repayments every week or month. Repayments varied by loan amount, but overall 22 per cent of Growth Fund borrowers in the survey repaid less than £10 per week on their Growth Fund loan, and a further 48 per cent paid between £10 and £19 per week (Table A3.18).

The majority of Growth Fund borrowers found it easy to repay their Growth Fund loan (89 per cent) (Table A3.19), and it was unusual for the borrowers in the survey to have missed payments. This seemed to be largely driven by payment method rather than repayment amount. The majority of borrowers repaid their Growth Fund loan by automatic deduction from benefits paid to the Growth Fund lender (44 per cent) or by direct debit (33 per cent) (Table A3.20). A relatively small proportion (17 per cent) made repayments in cash and these borrowers were more likely to say they had missed Growth Fund loan repayments.

3.4.2 Wider financial benefits of borrowing from the Growth Fund

The survey data indicated that a third of Growth Fund borrowers (34 per cent) reported that they felt better off financially as a result of borrowing from a Growth Fund lender (as opposed to raising the money some other way). Most, however, felt that their financial situation was about the same (58 per cent); very few (six per cent) felt that their overall financial situation had got worse as a result. In contrast, around two in ten (18 per cent) unsuccessful applicants reported that their situation had got worse (Table A3.21).

The Growth Fund borrowers who were interviewed in depth commonly identified wider benefits to their personal or family situation as a result of taking out a Growth Fund loan. One such benefit was to help relieve the personal anxiety or stress associated with managing on a low income. Typical comments included that the loan had "*reduced the pressure*"; that it "*helped take the financial strain away*", or that it "*removed a constant worry*". Borrowers often felt reassured that they could apply for a loan from the same lender again in future if needed. For those who were living with a partner or other family members, this reduction in anxiety or stress was sometimes reported to have had positive knock-on effects for their personal relationships.

3.5 The material benefits of borrowing from the Growth Fund

The Growth Fund borrowers that were surveyed generally planned to spend the money they borrowed to improve their household's standard of living. The most commonly reported purposes of Growth Fund loan applications were:

- Furniture, furnishings or decorating (reported by 30 per cent of borrowers)
- To pay for a birthday, Christmas or other special occasion (26 per cent)
- To pay for a holiday (12 per cent) (Table A3.22).

In the event that their Growth Fund loan application had been turned down, a third of borrowers (32 per cent) said they would have gone without the money and the items or services it would have allowed them to buy. A further 23 per cent said they would have taken no action (Table A3.23). Alternative courses of action that borrowers said they might have taken included: borrowing from friends and family (mentioned by 10 per cent of borrowers); home credit loan (nine per cent); try to save up (nine per cent); apply to the Social Fund (seven per cent) (Table A3.23).

As we go on to discuss in section 5.4, depth interviews with unsuccessful applicants indicated that they were not always able to borrow the full amount they wanted from friends or family when their Growth Fund loan application was turned down. The impact assessment analysis described in Chapter 7 uses the comparison group data to statistically model the counterfactual, i.e. what could we reasonably expect borrowers to have done in the absence of the Growth Fund.

Growth Fund borrowers were also asked about the ways in which they might raise £500 for something they wanted to buy sooner rather than later. Nearly eight in ten borrowers (77 per cent) said they would borrow from a credit union or CDFI, the most popular answer by a long way. The next most common response was to borrow from friends or family, mentioned by 28 per cent (Table A3.24). Together, these findings highlight the limited options for raising money open to these individuals and the important role that the Growth Fund has played in widening access to credit in deprived areas.

Box 2: The Growth Fund: A borrower's perspective

Yvonne is a lone parent in her 40s with three children. She is a full-time carer and her main source of income is Income Support. Yvonne heard about the Growth Fund lender she used from a friend. She needed money to pay for Christmas presents and clothes for her children, but her poor credit history meant that her only option was to borrow from family or friends which she was reluctant to do. She found the process of applying for a Growth Fund loan straightforward: she filled in a loan application form, provided evidence of her income and outgoings, and discussed her loan application with a credit union loan officer. Yvonne was awarded a £300 Growth Fund loan to be repaid over the course of a year, with repayments of £10.50 per week which she felt to be very reasonable. She also felt that the interest rate she was charged was *'very, very fair'* particularly compared with home credit loans that she had taken out in the past. As a result of this Growth Fund loan, Yvonne explained, '*my kids had a Christmas'*.

4 Other impacts of the Growth Fund on borrowers

Having looked in Chapter 3 at the impacts of the Growth Fund on borrowers' credit use, financial situation and standard of living, we move on in this chapter to explore some of the additional tangible benefits that the Growth Fund can bring to its customers (both successful and unsuccessful), over and above its main objective of widening access to lower cost credit. We start by looking at access to banking, before moving on to explore changes in saving behaviour. The final section looks at access to advice and changes to money management behaviour.

4.1 Banking

This section examines overall levels of banking among Growth Fund applicants. It then looks at the number of applicants who had taken out a bank account through a Growth Fund lender, and the extent to which Growth Fund applicants used their bank accounts.

4.1.1 Levels of bank account holding among Growth Fund applicants

Overall, eight in ten of all Growth Fund applicants (successful and unsuccessful) had a transaction bank account, with rather more having a basic bank account (45 per cent) than a current account (35 per cent). One in seven of all applicants (14 per cent) only had a Post Office Card Account (POCA), and a further six per cent had neither a bank account nor a POCA (Table A4.1). There were some differences between successful and unsuccessful applicants in terms of their account holding (for example, successful applicants were more likely to report having a full current account), but these were not great.

4.1.2 Take-up of bank accounts from Growth Fund lenders

Of the 24 Growth Fund lenders that applicants in the survey had used, ten offered access to a bank account. In most cases these were credit unions offering credit union current accounts. In addition, one CDFI worked in partnership with a bank to provide

access to bank accounts. This meant that 40 per cent of the applicants surveyed used a lender that offered a bank account.

Overall, 13 per cent of all Growth Fund applicants with a bank account had this account as a direct result of their contact with a Growth Fund lender (equivalent to 10 per cent of all applicants). This figure was higher among successful Growth Fund applicants than unsuccessful applicants. So, 16 per cent of successful applicants with an account had opened it through a Growth Fund lender compared with nine per cent of unsuccessful applicants with an account (Table A4.2).

4.1.3 Use of bank accounts

Growth Fund applicants (successful and unsuccessful) who had a transaction bank account seemed to make use of it, whether or not it had been opened with a Growth Fund lender. The most commonly mentioned uses were:

- To receive benefits, tax credits or earnings (mentioned by 88 per cent of account holders)
- To pay bills by direct debit or standing order (70 per cent)
- To withdraw cash from an ATM, bank branch or other location (70 per cent)
- To buy things with a debit card (41 per cent) (Table A4.3).

Just two per cent of account holders said they did not use their account at all (Table A4.3).

4.2 Saving

This section starts by looking at whether Growth Fund applicants had any money saved in savings accounts and the amounts they had saved (both in accounts and informally). It goes on to examine patterns of saving by Growth Fund applicants in accounts held with Growth Fund lenders.

4.2.1 Overall levels of saving among Growth Fund applicants

To gauge levels of saving at the household level, Growth Fund applicants were asked whether they or their partner had any money saved, either in an account or informally. Six in ten applicants overall (60 per cent) reported having no money saved at all. The

proportion without savings was much higher among unsuccessful than successful applicants (81 per cent compared with 46 per cent respectively) (Table A4.4).

Where applicants had money saved, the most common savings vehicle was a credit union account, mentioned by 26 per cent of all applicants (36 per cent of Growth Fund borrowers). Seven per cent of applicants had money saved in some other type of account, most often an ordinary savings account with a bank or building society. Less than one in ten applicants (seven per cent) had money saved informally, for example at home in a jar (Table A4.4).

Where Growth Fund applicants had money saved (formally or informally) the amounts were modest, so that four in ten of those with any savings (43 per cent) had less than £100 (Table A4.5). There was not a great deal of difference in the distribution of saving between Growth Fund borrowers and unsuccessful applicants. It was notable that more than a quarter (27 per cent) of Growth Fund borrowers with savings could not report the total amount they held in saving. The equivalent figure among unsuccessful applicants was only five per cent (Table A4.5).

4.2.2 Current patterns of saving with Growth Fund lenders

Overall, 21 of of the 24 Growth Fund lenders that applicants had used offered savings accounts, including one CDFI that offered savings account through an arrangement with a high street bank. This meant that the majority of applicants surveyed (84 per cent) had access to a savings account facility through their Growth Fund lender.

A third of all Growth Fund applicants in the survey (33 per cent) reported that they were actively saving into an account with their Growth Fund lender. This figure was much higher for successful applicants than unsuccessful (45 per cent compared with 14 per cent respectively) (Table A4.6).

In addition, 35 per cent of successful applicants were saving money with a Growth Fund lender on a regular basis, such as every week or month (Table A4.7). The typical (median) amount they saved was £5 per week. In contrast, only nine per cent of unsuccessful applicants were saving regularly with a Growth Fund lender, and the small number of savers precludes analysis of the amount being saved. Small numbers of applicants either saved with a Growth Fund lender as and when they could, or alternatively let their benefits build up in an account (Table A4.7).

Overall, the survey indicates that three in ten applicants (29 per cent) had savings in an account with a Growth Fund lender, but in no other account. For successful applicants, this figure was 40 per cent. Only a small proportion of applicants had savings with both the Growth Fund lender and elsewhere (four per cent) (Table A4.8).

4.2.3 What explains patterns of saving with Growth Fund lenders?

The qualitative interviews with Growth Fund borrowers provide further information about patterns of saving. Many of the successful applicants interviewed in depth said that they had opened a savings account with the lender when they took out the loan, to have benefits paid into the credit union from which loan repayments could be directly deducted. Having opened a savings account, applicants' saving behaviour was strongly influenced by the lender they used. While saving was by no means mandatory for borrowers, some lenders used 'soft compulsion' to encourage saving at the point of lending. This meant that, when the loan agreement was made, the lender routinely agreed with the borrower a set amount of money to be paid into savings by direct deduction at the same time as their instant access loan was being repaid.

Almost all of those Growth Fund borrowers who started saving in this way said they continued to save on a regular basis after receiving the loan, generally because once the arrangement was set up they took no further action. They found it straightforward to adjust their weekly expenditure to accommodate the combined loan repayment and savings contribution. They were often surprised by how quickly their savings built up over time, and how little they missed the extra amount once they had adjusted to a regular repayment pattern. Some were saving because they felt this would help them secure a higher value loan from the same lender in the future.

Among other successful Growth Fund applicants, who had not experienced this type of soft compulsion to save, the picture in relation to saving behaviour was mixed. Most had opted not to save on a regular basis after opening a savings account, mainly because they felt they had insufficient income to save while on a low income, although some would consider doing so at a later date. A few applicants were making regular financial contributions to family members instead of accruing any kind of savings.

4.3 Financial capability

This section starts by looking at whether Growth Fund applicants were offered any advice on money matters by Growth Fund lenders at the time when they applied for a loan. It then goes on to examine applicants' subjective views about the impact of their contact with a Growth Fund lender on aspects of money management.

4.3.1 Advice

The majority of Growth Fund applicants (84 per cent) reported that they had not been offered any advice on money matters by their Growth Fund lender. In the instances where advice was offered to applicants, it was more likely to be turned down than taken up. So, of the 16 per cent of applicants offered advice, only six per cent took it up (Table A4.9).

Among the small proportion of applicants who took advantage of the advice offered, the most common outcome was to have worked out a household budget to better manage their money. Other reported actions included switching utility company or insurance provider, and taking steps to sort out financial difficulties, such as setting up arrangements with creditors to pay back arrears.

As we go on to discuss in Chapter 5, most unsuccessful Growth Fund applicants said they were not referred to an advice agency when their loan application was turned down.

4.3.2 Money management

The survey asked Growth Fund applicants for their subjective views about changes to aspects of money management since they first started using the Growth Fund lender, including:

- Perceived changes to their money management skills
- Whether they felt more or less in control of their finances
- Whether they felt more or less financially secure
- Whether they felt more or less worried about money.

Among successful applicants, contact with a Growth Fund lender had often had a positive impact in these respects. Four in ten successful applicants (39 per cent) felt

their money management skills were better. Similar proportions said they felt more in control of their finances (41 per cent); more financially secure (39 per cent) and less worried about money generally (37 per cent). In all cases, the proportions of unsuccessful applicants reporting these positive changes were lower (16 per cent, 20 per cent, 14 per cent and 11 per cent respectively) (Tables A4.10-A4.13).

The qualitative interviews with successful Growth Fund borrowers indicated that having to adjust to a regular loan repayment pattern often required them to budget more effectively, particularly as the repayments tended to be deducted automatically from their income. Typical comments included that "*it has made me put that into a routine now*", and "*I'm a lot more careful with my money*". Linked to this, applicants often reported a greater sense of ownership of their finances, and were more likely to make a conscious effort not to overspend.

5 Unsuccessful Growth Fund applicants

This chapter starts by examining the reasons why applicants were turned down, based on the telephone survey of Growth Fund lenders. It goes on to explore whether or not unsuccessful applicants themselves knew why their application had been turned down, and whether they had been referred by the Growth Fund lender for advice. It then looks at the actions taken by unsuccessful applicants in the wake of their loan refusal, and their likelihood of applying to the same Growth Fund lender again. The final section draws on the qualitative interviews with Growth Fund lenders' about groups that might be un-served or under-served by the Growth Fund.

5.1 Why were Growth Fund loan applications turned down?

As we go on to discuss in Chapter 6, Growth Fund lenders used a combination of methods to assess Growth Fund loan applications, to ascertain whether or not a loan should be granted. These included information on applicants' income and expenditure, their current borrowing, and their past credit history (although a poor credit history would not necessarily preclude a successful application).

The telephone survey of Growth Fund lenders indicates that unsuccessful applicants may lack the capacity to repay a Growth Fund loan and require a solution other than borrowing. By far the most common reason for lenders to refuse a *first-time* Growth Fund loan application was because the applicant did not have sufficient disposable income to repay a loan (mentioned by 76 of the 82 lenders in the survey). The other reasons given by lenders included poor credit history (mentioned by 42 lenders); arrears on existing household bills and/or credit commitments (mentioned by 38 lenders); and the inability of applicants to provide appropriate forms of identification (mentioned by 49 lenders).

The purpose of the loan was also mentioned by a considerable number of the lenders as a reason for refusal. This included turning down first-time loan applications where the money was required to pay bankruptcy or similar fees (mentioned by 42 lenders); or where the reason for the loan was simply felt to be inappropriate (mentioned by 41

lenders). Several lenders (11 of the 82 surveyed) did not award loans for the purpose of debt consolidation.

In the case of *repeat* Growth Fund applications, the reasons for refusal followed much the same pattern as first-time applications, with insufficient disposable income to repay a loan again a key barrier to accessing a Growth Fund loan. However, having arrears on an existing Growth Fund loan, reaching the cap on the number of Growth Fund loans permitted per person (caps were operated by 46 of the 82 lenders that took part in the telephone survey), and the fact that applicants were still repaying an existing Growth Fund loan all featured among the main reasons why lenders refused repeat applications.

Several Growth Fund lenders (both in the telephone survey and the depth interviews) mentioned applicants' honesty as a major factor in loan decision-making. For example, if an applicant did not disclose outstanding debts on their application form or in an interview that subsequently came to light in a credit check, this might influence the loan decision.

5.2 Did unsuccessful applicants know why their loan application was refused?

Among the unsuccessful applicants surveyed, half (51 per cent) did not know why their application had been turned down. Where they were able to give a reason, the most common was the fact that they were in arrears with existing commitments (mentioned by 17 per cent). Having a poor credit history and low income were the most often mentioned after this (Table A5.1).

The depth interviews with unsuccessful Growth Fund applicants highlighted that it was common for applicants to receive notification of refusal by letter, without the reason for refusal being stated. Many of these applicants opted not to contact the lender for more information either because there seemed to be "no point" in following-up the letter, or because the applicant felt upset or annoyed at being turned down.

5.3 Were unsuccessful applicants referred to an advice agency?

Unsuccessful Growth Fund applicants in the survey were asked if they were referred to an advice agency by the Growth Fund lender when their loan application was turned down, for example to sort out any financial difficulties that they had. Most of them (79

per cent) said they had not been. Just over one in ten (12 per cent) said they had been referred for advice (Table A5.2).

The depth interviews with unsuccessful Growth Fund applicants suggest that the low levels of referrals might reflect the method of notification – those who received a letter by post usually said that this was their last point of contact with the lender. A few unsuccessful applicants who were notified of the loan decision by telephone were offered an appointment with a money adviser, but none of them took up this offer.

From the perspective of lenders, apart from offering money advice if an applicant was in financial difficulty, it might be difficult to know where to signpost unsuccessful applicants, except perhaps to charitable grant-giving organisations in certain circumstances. As one lender pointed out in the depth interviews, apart from their own organisation, there were no other sources of low-cost loans that they could refer people to - over and above the Social Fund which has strict eligibility criteria.

5.4 Actions taken by unsuccessful applicants when turned down

For the most part, unsuccessful loan applicants had applied to a Growth Fund lender for much the same things as successful applicants. The most often mentioned were paying for Christmas, birthdays or other special occasions (18 per cent of unsuccessful applicants) and buying furniture or fitting for their home (24 per cent). One in eight (13 per cent) of unsuccessful applicants had wanted a loan to pay household bills (Table A3.22).

The majority of unsuccessful applicants (72 per cent) said they did not take any action when their loan application to a Growth Fund lender was turned down – they simply went without the money and the things that they had intended to buy with it (Table A5.3).

Only eight per cent of unsuccessful applicants said they had used commercial credit to buy the things they had applied to the Growth Fund lender for. This was typically a loan from a home credit or other finance company. A further two per cent of unsuccessful applicants had applied for some type of commercial credit but been turned down (Table A5.3). None of the unsuccessful applicants in the survey reported using an unlicensed lender when their Growth Fund loan application was turned down.

In ten per cent of cases, unsuccessful applicants had either taken out a loan from the Social Fund or borrowed from a friend or family member. Depth interviews with unsuccessful applicants who had borrowed from a friend or family member indicated that they were rarely able to secure a loan to the value requested from the Growth Fund, and the total repayment period was thought to be longer. Some were uncomfortable with the strain that this put on relationships with people they knew, and saw this as being very much a "*last resort*".

Very few of the unsuccessful applicants in the survey (two per cent) had drawn on savings or tried to save up the money (Table A5.3).

5.5 Were unsuccessful applicants likely to re-apply to the same Growth Fund lender?

Most of the unsuccessful Growth Fund applicants that took part in the survey (70 per cent) had only ever made one loan application to that particular Growth Fund lender (Table A5.4). A small proportion (six per cent) said they had received at least one loan from the same lender, although this would not necessarily have been funded through the Growth Fund (Table A5.5).

When asked in the survey whether they would apply to the same Growth Fund lender again, most unsuccessful applicants (58 per cent) said they would. A quarter (26 per cent) said they would not, and the remaining 16 per cent were unsure one way or the other (Table A5.6). People's future intentions did not seem to vary greatly by the number of times they had already applied to the same lender.

Unsuccessful applicants were also asked whether or not they would recommend the Growth Fund lender they had used to someone they knew who needed a loan. Nearly six in ten unsuccessful applicants (57 per cent) said that they would recommend the lender, despite having been turned down themselves on at least one occasion; some of them had already made a recommendation. The equivalent figure was much higher among the successful applicants, with almost all of them (94 per cent) saying they would recommend the lender to someone else; indeed, most of them had already done so (Table A5.7).

5.6 Growth Fund lenders' views of un-served or under-served groups

The last section in this chapter draws on the telephone survey of Growth Fund lenders to explore their views about the types of financially excluded people they might not be reaching through the Growth Fund.

Around half of Growth Fund lenders in the telephone survey (42 of the 82 interviewed) considered that, within the area that their organisation covered, there were locations or (less commonly) groups of people that they were currently not serving. Among credit unions, this often meant areas outside their common bond, and some lenders mentioned the difficulties of serving large rural areas which had many small towns and villages or areas on the outskirts of large conurbations.

Lack of resources was the most commonly cited reason for not being able to serve these communities. When asked what they would require to deliver low-cost credit, not surprisingly the most common responses were more staff and/or volunteers and more loan capital. Some lenders also mentioned premises as a requirement, including more branches or collection points, a high street presence or financial support to pay for premises.

In addition, the Growth Fund lenders we interviewed in depth felt strongly that there was a need to continue to raise awareness and provide information to people on low incomes about the credit options available to them (including third sector lenders). Further efforts to link instant access loans to the provision of help and support around money matters more generally (such as saving, dealing with financial difficulties, budgeting, or getting the best deal) were also advocated as a means of helping people on low incomes achieve greater financial stability over the longer term. It was acknowledged that the development of this more rounded approach to money matters lay outside the remit and resources of the Growth Fund, however.

6 Impact of the Growth Fund on third sector lenders

This chapter draws on a telephone survey of 82 Growth Fund lenders and depth interviews with eight lenders to explore the impact of the Growth Fund on them. It starts by considering whether delivery of the Growth Fund had made third sector lenders more business-like in terms of the processes and procedures they employed.

Subsequent sections look at changes in the volumes of lending and customer profile as a result of the Growth Fund. The chapter then looks at whether lenders planned to continue lending to the Growth Fund's target group when the funding for Growth Fund ended in March 2011. The final section looks at funding more generally.

6.1 Were third sector lenders more business-like as a result of the Growth Fund?

Eight in ten Growth Fund lenders in the telephone survey (64 of the 82 that took part) reported that their organisation had improved its working practices as a direct result of the Growth Fund and now operated in a more business-like way. The challenges of an increased focus on capacity-based lending to potentially higher-risk borrowers had generally led lenders to tighten up their policies and procedures. This was often felt to have benefited the organisation as a whole. Sections 6.1.1 and 6.1.2 examine lenders' loan decision and arrears management processes. Section 6.1.3 looks at the impact of the Growth Fund in terms of the number of paid staff employed by lenders and the number of service points from which they operated.

In addition, several of the third sector lenders interviewed in depth considered that the Growth Fund had provided impetus for strengthening their Boards of directors, for example by taking on new directors; by directors becoming more engaged with the need for affordable credit among their customer base; or by fostering a more professional attitude and approach.

6.1.1 Loan decision process

Lenders in the UK are legally required to use sufficient information in order to assess potential borrowers' creditworthiness before granting credit or significantly increasing the amount of credit advanced.

The telephone survey and qualitative interviews indicated that Growth Fund lenders generally used a combination of methods to reach a decision about whether or not to grant a Growth Fund loan. These included the use of loan application forms to collect information such as applicants' employment status and their income and expenditure; interviews with prospective borrowers; and credit checks with credit reference agencies. Factors such as the purpose of the loan and applicants' honesty in providing the required information were taken into account when considering a loan application.

The telephone survey indicated that four in ten Growth Fund lenders (36 of the 82, and the largest single group of lenders) routinely interviewed first-time applicants and carried out a credit check, as well as collecting information via an application form. In addition to these methods, a further 22 lenders also credit scored first-time loan applications. Lenders were less likely to carry out these types of assessment for repeat Growth Fund applicants (Figure A6.1).

Seven in ten of Growth Fund lenders interviewed by telephone (59 of the 82 interviewed) reported that the application process was generally the same for non-Growth Fund as it was for Growth Fund loans. For the remainder who said it was different (28 of the 82 interviewed), the process for non-Growth Fund loans (which were typically savings-based) tended to be lighter-touch, for example applicants were not routinely credit checked; they were not required to have an interview; or in cases where they were interviewed, less information was required than for a Growth Fund loan.

The non-Growth Fund third sector lenders that took part in the telephone survey were much less likely to conduct routine credit checks or credit score applications. This was largely driven by the fact that most of them only offered savings-based loans. A few lenders in the comparison group did not interview, credit check or credit score even first-time applications, presumably making loan decisions based on the individual's saving history and/or the loan application form.

6.1.2 Arrears management and debt recovery processes

Some of the Growth Fund lenders interviewed in depth had tightened up their credit control processes in response to higher than expected levels of loan delinquency early on in their Growth Fund contract. The telephone survey indicated that eight in ten Growth Fund lenders (68 of the 82 interviewed) had a dedicated credit controller on their staff, at least some of whom would have been employed as a direct result of the revenue support they received from the Growth Fund. Around nine in ten Growth Fund lenders (72 of the 82 interviewed) monitored missed loan repayments at least weekly, and often daily. For the most part, the debt recovery process operated by the lender was triggered when one or two loan repayments had been missed (Figure A6.2).

In the depth interviews, Growth Fund lenders described fairly similar approaches to each other in terms of arrears management. The key, they felt, was to have a consistent approach and to be seen to follow-up missed payments quickly and effectively. The initial contact to follow up missed payments was generally by means of a telephone call or letter, in which the lender would seek to resolve the issue informally, for example by rescheduling the debt. If the borrower did not respond or failed to make a repayment within a set period of time, this would typically be followed up by a series of more formal letters to demand payment.

The telephone survey found that around two-thirds of Growth Fund lenders used an external debt collection agency if they did not receive payment as a result of their internal procedures. A few of the case study lenders had in-house debt collection staff. Where appropriate, around a third of Growth Fund lenders in the survey would routinely take court action to recover arrears on loans; a similar proportion only did so in exceptional circumstances.

Among the non-Growth Fund lenders that were surveyed, there seemed to be less onus on daily or weekly monitoring of missed repayments; a few of them monitored less often than monthly which was not the case for any of the Growth Fund lenders surveyed. In addition, rather more non-Growth Fund lenders said that their debt recovery process was triggered by two missed repayments rather than one.

6.1.3 Numbers of paid staff and service points

Data for Growth Fund lenders for the year 2004 (pre-Growth Fund), indicates that most of the lenders in existence at that time had at least some paid members of staff and delivered services from more than one location. On average, Growth Fund lenders employed more paid staff and increased the number of service points in both 2006 and 2009, once the Growth Fund got underway:

- The average (median) number of paid staff increased from 1.5 FTE in 2004, to 2.0 in 2006 and 4.0 in 2009.
- The average (median) number of service points increased from four in 2004, to six in 2006 and eight in 2009.

The average (median) number of volunteers stayed roughly the same (Figure A6.3). As a result, in 2009 we found that only one Growth Fund lender (a sub-contractor) had no paid staff at all, and only a handful operated from only one location. In terms of increasing an organisation's capacity more generally, the lenders interviewed in depth often felt these changes heralded positive benefits for their wider membership or customer base as well.

Rather fewer Growth Fund lenders provided data for *all* three years we asked about (2004, 2006 and 2009), and these tended to be larger lenders. If we only look at these lenders, the picture is very similar in terms of average (median) numbers of staff and delivery points. It shows that infrastructural changes were already underway to some extent in these organisations before the Growth Fund started in earnest in 2006 (Figure A6.4).

In total, 13 of the 25 non-Growth Fund lenders returned data for all three years in these dimensions. The data indicates that these lenders were in a fairly similar position to Growth Fund lenders in 2004 in terms of average (median) numbers of paid staff, volunteers and service points. In contrast to the Growth Fund lenders, however, their position remained fairly static over the next five years, particularly in relation to numbers of paid staff.

6.2 Volumes of lending

The data collected from the 82 Growth Fund lenders in the telephone survey indicates that more than half of them had made 500 or more personal loans in 2004; only a small number made less than 100 personal loans. The average (median) number of personal loans made (including both Growth Fund and non-Growth Fund loans) increased in 2006, and then particularly sharply in 2009. Looked at another way, there was a more than 200 per cent increase in the average volume of personal loans between 2004 and 2009 (Figure A6.5).

The average (median) total value of personal loans also increased in each of these years, from £159,032 in 2004, to £217,729 in 2006 and £411,000 in 2009. Reflecting the Financial Inclusion Taskforce's preference for Growth Fund loans in the region of £300 to £600, the average loan size for all personal loans in 2009 was lower (around £530) compared with 2006 (£815) and 2004 (£633).

Looking only at the Growth Fund lenders that provided data at all three points in time, it can be seen that although lending was already on the increase before 2006, the Growth Fund provided a significant stimulus for far greater volumes of lending (Figure A6.6).

Among the non-Growth Fund third sector lenders that returned data, it was notable that in 2004 the average total value of their personal lending was considerably higher than the Growth Fund lenders (with a median of around £329,000 compared with £159,032). Over the period 2004-2009, it remained relatively stable at around £0.3 million per year.

6.2.1 Debt write-off

Increased levels of debt write-off was one of several negative aspects of the Growth Fund that participating lenders identified in the telephone survey. Data provided by 28 lenders for all three years (2004, 2006, 2009) indicated that, on average, there was an almost nine-fold increase in bad debt write-off between 2004 and 2009: from an average (median) of £6,622 in 2004 to £11,162 in 2006 and £57,941 in 2009. This has to be viewed in context of the very significant increase in the volume of lending described above, however. It should also be noted that the lenders providing data for all three periods tended to be among the larger of the Growth Fund lenders in the telephone survey. A lack of equivalent data on debt write-off from the non-Growth Fund group of lenders precludes any comparison.

6.3 Customer profile

As Chapter 2 indicates, the main beneficiaries of the Growth Fund were women, people aged under 40, families with children (and single parents in particular), and people not in work. One of the main benefits of the Growth Fund from the lenders' perspective was that it had enabled them to lend to financially excluded people they had not previously served. As a result, most Growth Fund lenders in the telephone survey agreed that the customer profile of their organisation had changed significantly as a result of delivering the Growth Fund. Several of the lenders we interviewed in depth mentioned that they were now reaching far more young people than had previously been the case.

The data provided by the non-Growth Fund group of lenders indicated that most of them considered their users or members to be on low incomes and, like Growth Fund lenders, to be made up of families with children. They were roughly evenly divided into those that considered their members or users to be mainly women, and those who felt they served about equal numbers of men and women.

A lack of saving among Growth Fund borrowers was seen as one of the main downsides of the Growth Fund by lenders who took part in the telephone survey. There were mixed views about the extent to which Growth Fund borrowers were able to save, with lenders about equally divided in terms of those who agreed that most Growth Fund borrowers could not afford to save money from their income, and those who disagreed.

6.4 Would Growth Fund lenders continue to lend to financially excluded people post-2011?

The Government's Growth Fund is due to come to an end in March 2011, although the capital for on-lending provided to lenders through the Growth Fund can be retained as capital in the organisation as long as it is used to serve financially excluded people.

In this context, the telephone survey asked Growth Fund lenders how likely they were to continue lending to the financially excluded people they had reached through the Growth Fund, when funding ended in 2011. The response was largely positive, with nine in ten of the lenders (75 of the 82 interviewed) reporting that they were very or fairly likely to continue lending to financially excluded people, with most reporting that they were very likely to do so. These lenders generally considered that their volume of lending to

financially excluded people would stay about the same or increase after 2011. Some lenders thought that their volume of lending would decrease.

For the small number of lenders who said they were fairly or very *unlikely* to continue lending to financially excluded people after 2011 (seven of the 82 surveyed), the main issue was resources – their organisations would simply not be able to cover the costs of lending to financially excluded people once the Growth Fund had ended.

6.5 Were Growth Fund lenders dependent on grant funding?

The telephone survey found that six in ten Growth Fund lenders (53 of the 82 lenders interviewed) currently depended on grant funding to operate. The remainder generally reported being self-financing. From the available data, it was difficult to see any clear-cut differences between those describing themselves as self-financing and those that did not. Lenders with fewer assets and lower volumes of lending (possibly indicative of less time in operation) seemed to be more likely to be dependent on grant funding, however.

Most of the Growth Fund lenders that were reliant on grant funding (45 of the 53) considered it likely that their organisation would become self-financing in the future, although twice as many thought this to be fairly likely than very likely. About half of them (22 of the 45) envisaged being self-financing within two or three years, the rest either thought it would take four or more years or did not know. The remaining small number of Growth Fund lenders thought it not very or not at all likely that their organisation would be self-financing in the future. These lenders did not appear to share any particular features that might explain their views.

Additional financial resources (for example in the form of additional funding, or extra loan capital) was by far the most commonly mentioned type of support that lenders felt they required to become self-financing. Having extra paid staff was also important for some lenders. Other types of support were mentioned far less often, but included training and mentoring and having a business-minded board of directors. In addition, several factors in moving towards self-financing were raised by Growth Fund lenders in the depth interviews, including:

- The crucial importance of retaining interest from loans as a key means of income generation.

- Linked to this, a desire to develop employer-based lending to people in work, with the possibility of providing larger loans and payroll deduction for the repayment of loans (and also to pay money into savings).
- The potential for partnership and consortium working, to maintain volumes of lending and potentially achieve economies of scale.

Among the group of 25 non-Growth Fund third sector lenders, rather more described themselves as self-financing (15) than dependent on grant funding to operate (10). Those currently dependent on grant funding expressed mixed views about whether or not they were likely to become self-financing in the future. Again, additional resources were seen as the key to moving towards self-financing among those that saw it as a possibility.

6.6 Future funding

Growth Lenders in the telephone survey were asked their views about three possible sources of future funding: accessing funds on commercial terms; the possibility of local authorities providing financial support; and, for credit unions only, the possibility of lending above the current interest rate cap.

6.6.1 Accessing funds on commercial terms

There was little enthusiasm among Growth Fund lenders generally for the idea of accessing funding on commercial terms, such as a subordinated loan (one that is repayable only after other debts with a higher claim have been satisfied). Less than one in ten Growth Fund lenders in the telephone survey (six of the 82 interviewed) had ever accessed funding on commercial terms in the past. And seven in ten lenders (59 of the 82 interviewed) considered it was unlikely that they would access funding on this basis in the future. Being unable to afford the loan repayments and not wanting to commit to a monthly outgoing of this type were by far the most common reasons given. Some lenders also felt that their Board of directors would be against such a move.

6.6.2 The potential for local authorities to provide support after 2011

Local authorities were an important source of funding for both Growth Fund and non-Growth Fund third sector lenders. On the whole, Growth Fund lenders in the telephone survey seemed cautiously positive about the potential for local authority to provide

financial support for the provision of low-cost credit once the Growth Fund ended in 2011.

Over half of Growth Fund lenders (46 of the 82) felt there was potential for local authorities to fund their organisation to deliver low-cost credit to financially excluded people after 2011. There were two main reasons for lenders to think this: first, they already received financial support from one or more local authority; and secondly a view that local authorities should support financial inclusion initiatives (although they have no legal duty to do so). However, while these lenders felt there was *potential* for support from local authorities, some questioned whether the funding to do so would be available, particularly given the economic situation at the time of the survey (March-April 2010) and proposed public sector cutbacks.

The remaining lenders were roughly evenly divided into those who did not see local authorities as a potential future funding source (20) and those that did not know (16). Where lenders saw no potential for local authority funding, this was generally due to the fact that local authority budgets in their areas had already been cut back.

6.6.3 Changes to the credit union interest rate cap

An increase in the statutory maximum rate of interest that credit unions can charge was introduced following the 2005 Pre-Budget Report, from one per cent to two per cent per month on the reducing balance of a loan. Many credit unions were charging in the region of two per cent on Growth Fund loans. There is currently no cap on the interest rates charged by community development finance institutions.

The telephone survey asked Growth Fund credit unions if they would consider lending above the current two per cent per month interest rate cap, if they were legally allowed to do so. There was little appetite for this idea. Around seven in ten (51 of the 77 credit unions interviewed) felt it was unlikely that they would consider lending above two per cent per month. That left only around a third of credit unions who considered it likely that they would lend above two per cent if the opportunity arose.

Among the non-Growth Fund third sector lenders that took part in the survey, their core business was generally savings-based loans. As a result, they were often charging lower interest rates than the current cap of two per cent per month. Almost all of these 25 lenders felt strongly that they were unlikely to charge above two per cent per month if this was legally possible.

6.7 Working with Growth Fund lenders: the views of other community organisations

The qualitative case studies in eight Growth Fund areas included interviews with representatives of 15 organisations that were involved in the delivery of services to financially excluded people in those areas. They were mostly frontline service providers and included representatives of advice agencies, social landlords, and regeneration agencies. The findings presented here represent people's views of working with Growth Fund lenders, rather than the Growth Fund itself. They provide additional evidence of the potential impact of Growth Fund lenders' within deprived local communities.

6.7.1 Examples of partnership working

Among the organisations we interviewed, the most common activities undertaken in partnership with Growth Fund lenders were: marketing and promotion of Growth Fund lenders' services; the referral of clients or service users to the Growth Fund lender, typically to apply for a loan; joint working with Growth Fund lenders to deliver services. For example, one Growth Fund credit union provided information materials for a community organisation to deliver to its service users, and would take referrals from the organisation as well. Another community organisation provided staff and premises for a credit union service point.

A few housing organisations provided direct grant funding to Growth Fund lenders to support the lenders' service delivery. One organisation (again a housing provider) had seconded a member of its staff to a Growth Fund lender to assist with marketing, and had also supplied expertise in the form of advice around IT and credit control processes and procedures.

In some instances, these working arrangements were on a formal basis, for example through a service level agreement or a memorandum of understanding. More commonly, however, there was no formal agreement in place.

6.7.2 Benefits of partnership working

The organisations we spoke to were overwhelmingly positive about their working relationships with Growth Fund lenders, and considered that the arrangement was

beneficial both to the organisation and its service users. None of the respondents reported any negative impacts on their own organisations.

For some organisations, there were strategic benefits of working with Growth Fund lenders, such as meeting targets around partnership working, or contributing to the organisation's wider financial inclusion strategy. At an operational level, the Growth Fund lenders offered a useful source of referral for the organisations' service users who could benefit from access to lower-cost credit. Among housing providers, this was perceived to be linked to a reduction in rent arrears among tenants who had more disposable income as a result of borrowing at a lower cost - although respondents acknowledged this was difficult to prove.

> *Main areas where we notice [a difference] – tenancy breakdown, debt, rent arrears, a need to purchase furniture before they move in and abandoning the property before they even get it. Whereas with the instant loans, they have enough money to buy a bed, cooker etc. so that they can move in.*

Similarly, a few respondents talked about anecdotal reports of a reduction in the use of high-cost lenders such as home credit companies in areas where a high penetration of people used Growth Fund lenders.

7 The costs and benefits of the Growth Fund

This chapter sets out an analysis of the costs and benefits of the Growth Fund between 2006 and September 2010. The analysis is based on administrative and financial data provided by the DWP, and an assessment of the interest savings accruing to Growth Fund borrowers and potential effects on their ability to obtain credit. This analysis has been undertaken in accordance with principles of the HM Treasury's Green Book, which sets out guidance for evaluation and appraisal in Central Government.

7.1 Costs

This section outlines the total costs associated with the Growth Fund, comprising the social costs of lending and administrative costs incurred by the DWP and Growth Fund lenders.

7.1.1 Social Costs of Lending Activity

The social costs of the Growth Fund involve two main elements:

- **Opportunity cost:** Providing capital for lending involves committing resources that could have otherwise been invested elsewhere. This opportunity cost is valued at 3.5 percent per annum, in line with the discount rate outlined in the HMT Green Book (which is intended to measure the rate of social time preference, but can also be interpreted as the opportunity cost of capital).
- **Cost of defaults on loans:** Where borrowers default and outstanding loan balances written off, there is a direct cost to the public sector in the form of lost capital.

DWP monitoring information provides only cumulative figures for total capital employed and loans written off, making direct estimates of the annual social cost of lending difficult. These costs have instead been inferred on the following basis:

- **New loan capital:** At the beginning of each year, new loan capital is added to the total stock by the DWP (this is a simplifying assumption; in reality new loan

capital is released on an on-going basis to meet demand). £59.3m in loan capital was employed between 2006/07 and September 2010.

- **Value of loans:** Annual information is available on the total value of loans distributed by Growth Fund contractors. £137.2m (excluding interest) was lent between 2006/07 and September 2010.
- **Repayment terms:** Information on interest rates charged is not available annually, though Growth Fund loans are typically associated with an APR of 26.8 percent. Most initial loans to borrowers were lent on these terms; subsequent loans were sometimes lent at a lower rate, while CDFIs sometimes lent at higher rates. An average APR of 26.8 percent has been assumed, and all loans are assumed to be distributed at the beginning of the year and repaid within that year, leading to an estimate that £36.8m of interest was due on loans made between 2006/07 and 20010/11.
- **Default rate:** DWP monitoring information suggests £7.8m of loans have been written off since 2006/07 (including interest payable on outstanding payments), equating to a default rate of 4.5 percent. Annual information on defaults is unavailable (though evidence indicates rates have fallen as the initiative progressed), so this rate is assumed to apply throughout the period.
- **Capital and interest repaid, and write downs on capital:** Applying the assumed default rate, it is estimated that capital repayments of £131.1m have been made (with interest payments of £35.1m), and total write downs on loan capital are estimated at £6.2m.
- **Transfer of interest and excess capital:** Growth Fund lenders can apply to the DWP to transfer interest income or excess loan capital for the purposes of running the scheme. In June 2010, transfers of £5.8m in interest income and £3.5m in excess capital were made. Transfers are assumed to represent a constant share of interest income or capital employed over the period (18 percent and 6 percent respectively).
- **Loan capital at the end of the year:** The value of capital employed is estimated by loan capital at the beginning of the year plus interest income, less write downs on capital and transfers[3].

[3] The opportunity cost of capital is applied to loan capital at the end of the year. This could also be applied to average capital over the course of the year, to reflect the assumptions made about the term times of the loan, although this would have little material impact over the results.

Results are set out in the table below, with the total social cost of lending estimated at £14.3m.

Table 7.1 Social Costs of Lending Activity

	2006/07	2007/08	2008/09	2009/10	2010/11	Total
New loan capital (£m)	9.3	20.4	8.2	12.7	8.7	59.3
Total loan capital, beginning of year (£m)	**9.3**	**30.3**	**41.6**	**59.0**	**74.1**	**-**
Lending						
Value of loans (excluding interest, £m)	7.7	26	31.9	43.5	28.1	137.2
APR (%)	26.8	26.8	26.8	26.8	26.8	-
Interest due (£m)	2.1	7.0	8.5	11.7	7.5	36.8
Total repayments due (£m)	9.8	33.0	40.4	55.2	35.7	174.0
Repayments						
Default rate (%)	4.5	4.5	4.5	4.5	4.5	-
Value of write downs on capital (£m)	0.3	1.2	1.4	2.0	1.3	6.2
Interest payments received (£m)	2.0	6.7	8.2	11.1	7.2	35.1
Transfer of interest and excess capital						
Percentage of interest income transferred	18.4	18.4	18.4	18.4	18.4	-
Interest income transferred (£m)	0.4	1.2	1.5	2.0	1.3	6.5
Percentage of excess capital transferred	6.1	6.1	6.1	6.1	6.1	-
Excess capital transferred (£m)	0.6	1.2	0.5	0.8	0.5	3.6
Total loan capital at the end of the year	**10.0**	**33.4**	**46.3**	**65.3**	**78.1**	**-**
Opportunity cost of capital (£m)	0.3	1.2	1.6	2.3	2.7	8.2
Value of write downs on capital (£m)	0.3	1.2	1.4	2.0	1.3	6.2
Total social costs of lending activity (£m)	**0.7**	**2.3**	**3.1**	**4.2**	**4.0**	**14.3**

Source: DWP Monitoring Information & ECORYS analysis

7.1.2 Administrative costs

The delivery of the Growth Fund has also involved resource costs in terms of DWP management of the scheme and capital and revenue expenditure of credit unions and CDFIs delivering the Growth Fund (as well as transfers of interest income and excess capital for revenue and capital expenditure). Total administrative costs are estimated at £40.8m[4].

[4] These figures exclude a £281,000 payment for consultancy unrelated to the initiative in 2008/09.

Table 7.2 Administrative Costs (£m)

	2006/07	2007/08	2008/09	2009/10	2010/11	Total
DWP administrative costs						
Staff costs	0.7	0.8	0.7	1.0	0.5	3.7
Non-staff costs	0.1	0.2	0.3	0.2	0.1	0.9
Growth Fund lender expenditure[5]						
Revenue expenditure	1.7	4.9	2.9	4.7	8.5	22.7
Capital expenditure	0.5	0.4	0.4	1.0	0.9	3.2
Transfers of interest income and excess capital	0.9	2.5	2.0	2.8	1.9	10.1
Total	**4.0**	**8.8**	**6.6**	**9.6**	**11.9**	**40.8**

Source: DWP Monitoring Data

7.1.3 Costs to commercial lenders

The Growth Fund also carries a potential disbenefit through crowding out commercial lenders in the private sector (if Growth Fund borrowers switch their borrowing from the private to the public sectors as a result of lower interest rates). This social cost will be felt in the form of foregone profits on lending that have been crowded out. The impact assessment suggested that when compared to the comparison group, the Growth Fund helped to displace credit from a range of sources, including the highest cost lenders (home collection lenders and pawnbroker loans), but also a range of other forms of credit including bank loans, finance company loans and hire purchase.

The average gross profitability of UK non-financial corporations (as a percentage of capital consumed) was 12.7 percent per annum between the beginning of 2006/07 and quarter 1 2010. A review of competition amongst high cost lenders undertaken by the OFT in 2009/10 also indicated that firms tended to earn a rate of return on capital employed slightly higher than the cost of capital employed (estimated at the upper end of a range from 8 to 11 percent), suggesting average profitability in the unsecured consumer lending sector reflects rates across the wider economy.

Additionally, the impact assessment indicated that Growth Fund may have had the effect of shortening the time period over which total debt is repaid by close to 9 months. If borrowers would have otherwise taken out loans or other borrowing over a period of 21 months (in comparison to the 12 months associated with Growth Fund loans),

[5] Subsequent analysis assumes this reflects the marginal cost of delivering the Growth Fund.

commercial lenders would have been likely to earn additional profits on the loan employed reflecting the greater opportunity cost.

Assuming this rate of return can be applied to the volumes of unsecured consumer lending crowded out, it is estimated that the Growth Fund resulted in a loss of profits for commercial lenders over 12 months of between £17.4m (if all Growth lending represents crowding out) and £12.2m (if 30 percent of Growth Fund borrowers would not have obtained credit at all – see below). If loans are assumed to be crowded out over 21 months, this rises to between £30.5m and £21.3m.

Some of these profits may have accrued to unlicensed or illegal lenders. However, survey evidence from both the successful and unsuccessful Growth Fund applicants as well as the comparison group suggests that usage of such lenders is highly limited, and no further adjustments are made.

Table 7.3 Loss of Profits to Commercial Lenders

Financial Year	2006/07	2007/08	2008/09	2009/10	2010/11	Total
Value of loans crowded out (excluding interest, £m)	7.7	26	31.9	43.5	28.1	137.2
Loans crowded out over 12 months						
Loss of profits for commercial lenders (£m, high)	1.0	3.3	4.1	5.5	3.6	17.4
Loss of profits for commercial lenders (£m, low)	0.7	2.3	2.8	3.9	2.5	12.2
Loans crowded out over 21 months						
Loss of profits for commercial lenders (£m, high)	1.7	5.8	7.1	9.7	6.3	30.5
Loss of profits for commercial lenders (£m, low)	1.2	4.0	5.0	6.8	4.4	21.3

7.2 Benefits

This section explores the benefits accruing to Growth Fund borrowers (in terms of total borrowing and interest paid), and the wider social benefits and disbenefits of the initiative.

7.2.1 Impacts on total borrowing and interest rates paid

By offering loans at lower interest rates than might otherwise obtain commercially, the Growth Fund will potentially generate benefits for borrowers through two main mechanisms:

- **Interest rate savings to Growth Fund borrowers:** As the Growth Fund is a loan scheme that aims to provide loans at lower interest rates than might accrue commercially, interest rate savings accruing to borrowers should be considered as a social benefit.
- **Increasing total borrowing:** If borrowers opt to choose – or are able to secure – a larger volume of credit as a result of lower interest rates, they will also gain an additional welfare benefit as they would have been willing take on at least some additional credit at higher interest rates[6].

The Growth Fund has also been designed to widen access to financial services amongst borrowers. However, it is assumed that the primary financial benefits of these outcomes will be captured in the measures above (though borrowers may accrue a range of less tangible benefits, such as reduced anxiety).

7.2.1.1 Interest rate savings

Comparisons of the interest paid on their total borrowing by Growth Fund borrowers to that paid by residents of non-Growth Fund areas (serving as a comparison group) indicated the former saw the total interest they paid over the lifetime of their current credit obligations reduced by between £377 and £425 per borrower, with between £130 and £154 coming from lower interest rates paid on borrowing, and the remainder being derived from a shortening of the period over which debt was repaid[7].

DWP monitoring data indicates 317,800 Growth Fund loans had been made between 2006/07 and 2010/11, giving an estimate that total interest savings accruing to borrowers could total between £119.8m and £135.1m over the lifetime of their current credit commitments, of which between £41.3m and £48.9m are driven by interest rate savings. Which of these represents the best estimate of welfare benefits accruing to Growth Fund borrowers depends largely on how far borrowers prefer the time profile over which Growth Fund loans are repaid to the terms set by commercial lenders.

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[6] I.e. a consumer surplus.
[7] See appendix for detailed description of how these estimates were derived.

Table 7.4 Interest Savings Accruing to Growth Fund Borrowers

Financial Year	2006/07	2007/08	2008/09	2009/10	2010/11	Total
Number of loans made	18,538	57,929	74,752	100,858	65,721	317,798
Low estimate						
Total interest savings (£m)	7.0	21.8	28.2	38.0	24.8	119.8
Total savings as a result of reduced interest rates (£m)	2.4	7.5	9.7	13.1	8.5	41.3
High estimate						
Total interest savings (£m)	7.9	24.6	31.8	42.9	27.9	135.1
Total savings as a result of reduced interest rates (£m)	2.9	8.9	11.5	15.5	10.1	48.9

7.2.1.2 Impacts on total borrowing

Analysis of the total borrowing decisions of Growth Fund borrowers and the control group could find no significant effect of the Growth Fund on the total amount borrowed[8]. This suggests that those benefitting from a Growth Fund loan would have generally obtained similar levels of credit from higher cost lenders in the private sector in the absence of the initiative, and implying demand for credit is relatively inelastic among those accessing Growth Fund loans. This reinforces the findings of studies elsewhere (such as the OFT's review of competition among high cost credit suppliers) that suggest borrowers frequently consider the affordability of monthly or weekly repayments rather than the total cost of credit.

However, respondents to the survey were also asked to report how they would have obtained credit if their application for a Growth Fund loan had been turned down (as outlined in Chapter 3). Some 30 percent of respondents reported they would not have accessed additional credit suggesting that this sub-group of the population of borrowers may have increased their borrowing as a result of the Growth Fund in way that was not captured through aggregate analysis.

The consumer surplus benefits gained by these borrowers have been estimated on the basis of the reduction in interest rates created by the Growth Fund and the average size of loans distributed (£432), and is estimated at £12.30 per borrower[9]. On the assumption that 30 percent of Growth Fund borrowers would not have taken up credit from another

[8] See Appendix for detail discussion of results.
[9] Using the rule of a half: the increase in consumer surplus = ½ x [Change in Interest Rates] x [Change in Total Borrowing]

provider in the absence of the Growth Fund, total welfare benefits resulting from individuals being able to extend their borrowing are estimated at £1.2m.

Table 7.5 Potential Consumer Surplus Benefits

Financial Year	2006/07	2007/08	2008/09	2009/10	2010/11	Total
Total number of loans made	18,538	57,929	74,752	100,858	65,721	317,798
Number of loans made to those that would not have taken up credit elsewhere	5,561	17,379	22,426	30,257	19,716	95,339
Total increase in consumer surplus (£m, low)	0.1	0.2	0.2	0.3	0.2	1.0

7.2.2 Hire purchase

The patterns of borrowing reported by Growth Fund borrowers indicated that the Growth Fund to some extent displaced credit taken in the form of Hire Purchase. This may have resulted in further savings if borrowers were able to purchase goods at a lower cost as a result of the Growth Fund opening up a wider range of choices. However, this was to some extent an unanticipated effect, and survey evidence did not directly address this issue, so it is not possible to examine these types of effect with precision.

7.2.3 Handling of defaults

While defaults on Growth Fund loans represent a cost to the public sector, they arguably represent a financial benefit to the borrower. However, defaulting on a loan will have a range of disbenefits to the borrower, including increasing the cost of or reducing their ability to obtain credit in the future. It is assumed that such borrowers are indifferent between the current financial benefit of defaulting on their loan and the expected future cost in terms of their ability to secure credit, so there is no net welfare benefit or cost to those defaulting.

7.2.4 Productivity improvements

One of the largest costs associated with the Growth Fund is the revenue and capital resources utilised by Growth Fund lenders in the delivery of the initiative. These resources (and in particular the capital expenditure) as well as DWP management of the initiative, may have helped them improve their productivity and efficiency in assessing the credit risk of borrowers, which would be reflected in a reduction in default rates. As highlighted in Chapter 7, the evidence is not sufficiently strong to suggest that

productivity improvements (in the form of reduced default rates) have been achieved at an organisational level as a result of the Growth Fund, and no adjustment has been made for productivity improvements.

7.2.5 Distributional effects

The Growth Fund has been targeted at those on lower incomes, who have a higher rate of marginal utility from consumption and will experience a greater benefit from interest rate savings than those on higher incomes. The HM Treasury Green Book recommends that where the benefits and disbenefits accruing to different income groups are known, they should be weighted in line with the marginal utility of their consumption.

The table below sets out the profile of Growth Fund by household type and income quintile (based on survey results and the appropriate income ranges set out in the Green Book), and shows that borrowers tended to be concentrated were primarily in the 1st and 2nd income quintiles (i.e. the 40 percent of the population with the lowest incomes). Applying the distributional weights set out in the Green Book, the benefits accruing to this group should be valued between 70 percent and 80 percent more highly than their monetary value to reflect this.

Table 7.6 Income Quintiles of Growth Fund Borrowers and Distributional Weights

Income Quintile	**Single, no child**	**Couple, no child**	**Single, 1 child**	**Couple, 1 child**	**Single, 2+ children**	**Couple, 2 plus children**	**Total**	**Dist. Weight**
1	50	40	73	41	44	57	52	2.2 – 2.3
2	32	34	0	28	40	22	27	1.4 – 1.5
3	0	0	21	12	11	13	9	1.0 – 1.1
4	13	19	5	14	4	9	10	0.7 – 0.8
5	4	07	2	5	1	0	3	0.4 – 0.5
	100	100	100	100	100	100	100	1.7 – 1.8

Applying an a distributional weighting of 75 percent (the midpoint of the estimated range) suggests that the Growth Fund could have led to further distributional effects valued at between £89.9 and £101.3m if all financial savings are treated as a benefit, and between £31.0 and £36.7m if any savings due to interest rate savings are treated as a benefit.

Table 7.7 Distributional Effects

Financial Year	2006/07	2007/08	2008/09	2009/10	2010/11	Total
Treating all financial savings as a benefit						
Distributional Effects – (£m, low)	5.2	16.4	21.1	28.5	18.6	89.9
Distributional Effects – (£m, high)	5.9	18.5	23.8	32.1	20.9	101.3
Treating only savings due to interest rate reductions as a benefit						
Distributional Effects (£m, low)	1.8	5.6	7.3	9.8	6.4	31.0
Distributional Effects (£m, high)	2.1	6.7	8.6	11.6	7.6	36.7

7.3 Conclusions

This analysis of the costs and benefits of the Growth Fund suggest that[10]:

- The cost of the administering the scheme totalled £40.8m, with the additional social cost of lending (i.e. the opportunity cost of lending to borrowers) estimated at £14.3m.
- The scheme also displaced the profits of commercial lenders (including both high cost home collection lenders as well other credit providers such as banks and hire purchase companies). These displaced profits are estimated to total between £12.2m and £17.4m if profits are assumed to be displaced over the 12 months. However, the evidence suggested that one of the effects of the Growth Fund was to help borrowers repay their debts over a shorter period (up to 9 months), in which case estimated profits displaced rises to £21.3m to £30.5m.
- The Growth Fund was found to have reduced the interest paid by Growth Fund borrowers on their lending through two mechanisms: reducing the interest rate paid on borrowing, and as noted, shortening the period over which borrowers repay their debts. Total interest savings are estimated at between £377 and £425 per borrower, and between £119.1m and £135.1m, of which between £41.3 and £48.9m represent interest rate savings. Which of these represents the best estimate of welfare benefits accruing to Growth Fund borrowers depends largely on how far borrowers prefer the time profile over which Growth Fund loans are repaid to the terms set by commercial lenders.

[10] The original terms of reference for the study was to develop a Cost-Benefit Analysis, but it was subsequently agreed that the costs and benefits would not be brought together in the form of a Benefit-Cost Ratio.

- The impact assessment did not suggest that the Growth Fund had an effect on the total amount borrowed. However, evidence from Growth Fund borrowers alone suggested that 30 percent may have done without credit in the absence of the fund. If this is the case, then this group are estimated to earn an additional welfare benefit of up to £1.2m.
- Additionally, the Growth Fund was mainly accessed by those in lower income groups, implying there is further distributional effect (on the basis that lower income groups place a higher value on additional income than higher income groups) of between £89.9m and £101.3m if the total financial saving is treated as a benefit, and between £31.0m and £36.7m if only the savings due to interest rate reductions are treated as a benefit.

There are a range of caveats associated with the analysis. Although estimates of the effects of the Growth Fund on the interest paid by individuals were statistically significant, the models did not explain a high share of overall variation in interest paid by borrowers. Estimates were based on the borrowing and repayment terms reported in the survey, and are likely to be subject a degree of measurement error, contributing to high variance in the models. It is also likely that there were omitted variables that were unaccounted for, including individual factors (such as discount rates and relative risk aversion) and contextual factors that influence borrowing decisions and interest rates faced by borrowers. Macro-economic developments over the period, with increasingly constrained credit supply and a large drop in the risk-free interest rate, are likely to be influential.

Benefits have also only been considered over the lifetime of the Growth Fund loans. If borrowers benefit on permanent basis (for example, if credit ratings improve as a result of repaying the loan enabling a lower cost of borrowing in the future) then overall benefits will be likely to be higher than estimated here. These may be particularly important if some of the secondary outcomes targeted by the intervention, such as widening access to financial services amongst the financially excluded help contribute to more effective management of personal finances on a longer term basis.

7.4 Estimating a commercial rate of return

As an addendum to this analysis, consideration has been given to the interest rate that Growth Fund borrowers would need charge in order to generate a commercial rate of return. In order to generate a commercial rate of return, expected interest income will need to cover operational costs, expected defaults on loan capital, and potentially generate a profit.

On an average loan size of £432 at the median APR of 26.8 percent, an interest income of £55.60 can be expected over a 12 month repayment term with a reducing monthly balance (factoring in a default rate on repayments of 4.5 percent)[11]. Lenders have spent (excluding the cost of DWP management) £36.0m in operational costs to distribute 318,000 loans, equating to an average of £113 per loan[12]. Given the default rate of 4.5 percent, the expected value of default on loan capital has averaged £19.40 per loan[13]. Taking these together, Growth Fund lenders have operated at a net loss of £77.20 per loan[14].

Higher interest rates would be needed to put Growth Fund lending on a more stable commercial platform. Assuming operational costs, risks associated with lenders, and average loan sizes remain constant, it is estimated that an APR of 71.2 per cent would be required to cover operational costs and financial risks associated with lending[15]. An APR of 108.2 per cent would be required to reach a commercial rate of profit of 12.7 percent on loan capital[16].

[11] i.e. 12 x ((£432 x 0.02 x (1 + 0.02) ^ 12) / ((1 + 0.02) ^ 12 – 1) - £432) x (1 - 0.045)
[12] i.e. £36.0m / 318,000 = £113.37
[13] i.e £432 x 0.045 = £19.40
[14] i.e. expected interest income (£55.60) – expected cost (£113.40 + £19.40 = £132.77) = -£77.20
[15] The total expected cost of lending (operational costs and default risk) on a £432 loan is £132.77, and an APR of around 71 percent would be required to deliver this level of interest.
[16] Interest would need to cover the expected cost of lending of £132.77, and generate an additional £54.8 in the form of a 12.7 percent profit margin on the loan (again factoring in an expected default rate of 4.5 percent), requiring an APR of around 108.2 percent.

Table 7.8 Rates of return required to break even or generate a profit – new lenders

	Current rates of interest	Income neutralitly	Commercial rate of profit
Loan size (£)	431.8	431.8	431.8
Monthly interest rate (%)	2.0	4.6	6.3
APR (%)	26.8	71.2	108.2
Interest due (£, assumed 12 month term)	55.6	132.8	187.6
Cumulative interest rate (%)	13.5	32.2	45.5
Expected value of default (£)	19.4	19.4	19.4
Cost of operations (£)	113.4	113.4	113.4
Net income per loan (£m)	-77.2	0.0	54.8

The higher interest rates are primarily needed to cover the £113 estimated operational cost. These costs are based on all operations expenditure from 2006 to 2010, and include all set up costs relating to setting up the Growth Fund, including initial capital expenditure, recruitment, and potentially establishing new premises. Additionally, many of the lenders involved have delivered administrative efficiencies in distributing the Growth Fund, so the interest rates set out in Table 7.8 above are more appropriate for considering the interest rates required to break even or generate a profit where an inexperienced or new lender were to begin delivering the Growth Fund.

By 2010, the operational costs of lending have fallen in the majority of cases to between to £60 and £75 per loan, reflecting both lower capital expenditure and increased administrative efficiencies. For current Growth Fund lenders, the required APRs to cover these costs are therefore estimated at:

- 39.6 per cent at £60 per loan to break even
- 48.1 per cent at £75 per loan, to break even
- To generate a 12.7 per cent rate of profit, the equivalent rates would be 72.0 percent at £60 and 81.7 percent at £75.

Table 7.9 Rates of return required to break even or generate a profit – current Growth Fund lenders

Operational Cost Per Loan	APR required to break even	Commercial rate of profit
£60	39.6	72.0
£75	48.1	81.7

These rates of return are lower than the rate suggested by research carried out for the Joseph Rowntree Foundation (JRF) for establishing a not-for-profit home credit lender (125 percent)[17], and these estimates may be considered as a minimum APR chargeable to cover costs for the following reasons:

- **Set-up costs:** The analysis does not account for any set-up costs that may be incurred, for example, if the interest was to develop a similar initiative without using the existing credit union and CDFI infrastructure. Higher APRs would be required to cover such costs, but as the Growth Fund has utilised existing organisations, there is no evidence available to base such an analysis on. The JRF research, for example, included recruitment and set-up costs in their modelling of the APRs required to set up a not-for-profit home collection lender.
- **Mode of delivery:** The JRF report is based on a home collection loan model that involves substantial agent costs in generating customers and collecting revenue. The Growth Fund is not based on such a model, so staffing costs will be lower.
- **Additional resource costs:** If third sector lenders have incurred any additional resource costs in delivery of the Growth Fund (staffing or capital) then these are not reflected in the APRs suggested. Again, accommodating such costs would imply a higher APR on lending.
- **Impact on default rates:** The analysis assumes that default rates remain constant as APRs increase. However, it is plausible that an increase in APRs could result in an increase in the default rate, and potentially more resources expended in chasing such loans. Again, this would entail higher APRs than suggested.

[17] E. Kempson, A. Ellison, C. Whyley and P.A. Jones (2009). *Is a not-for-profit home credit business feasible?* Joseph Rowntree Foundation

8 Summary and conclusions

The objective of the DWP Growth Fund was to raise levels of access to affordable credit by building the capacity of third sector lenders to serve financially excluded households. In doing so, the Growth Fund aimed to disrupt the role of high cost credit in the lives of borrowers. The evaluation aimed to establish the following impacts of the Growth Fund on Growth Fund borrowers and lenders:

Group	Impact Measures
Borrowers	Propensity to use high-cost or illegal credit
	Access to, and use of, appropriate financial services
	Savings on interest payments
Growth Fund Lenders	Overall customer profile
	Lending practices
	Levels of business and capacity
	Use of other streams of funding

This final chapter starts by assessing whether the Growth Fund increased access to affordable credit among financially excluded households. It then brings together the evaluation findings in relation to each of the impact measures outlined above. The last section outlines the findings from a detailed analysis of the costs and benefits of the Growth Fund.

8.1 Did the Growth Fund increase access to affordable credit?

The Growth Fund was targeted at financially excluded people living in deprived communities across Britain where there was evidence of a mismatch between the demand for and supply of affordable credit. DWP statistics indicate that 317,798 Growth Fund loans were made in deprived communities from July 2006 up to the end of September 2010, with a total value of over £137 million. An additional 12,090 loans were made in October 2010. Volumes of personal lending reported by Growth Fund credit unions and CDFIs increased by more than 200 per cent between 2004 (prior to the Growth Fund) and 2009 (see section 8.3.3.1).

The survey data indicated that, once someone had successfully applied for a Growth Fund loan, they were very likely to apply to the same lender again. 68 per cent of Growth Fund borrowers in the survey had applied for loans on two or more occasions, usually successfully. These subsequent loans were not necessarily funded by the Growth Fund, and the telephone survey of lenders found that non-Growth Fund loans were generally offered at lower rates of interest, typically around 12 per cent APR.

The majority of successful Growth Fund borrowers (95 per cent) said they would apply to the same Growth Fund lender again if they needed another loan. A similar number (94 per cent) said they would recommend the lender to someone else and indeed many of them had done so. Despite having been turned down for a loan, 58 per cent of unsuccessful Growth Fund applicants said they would apply to the same lender again; 57 per cent said they would recommend the lender to someone else.

8.1.1 Did the Growth Fund reach its target audience?

Analysis of the survey data collected for this evaluation indicates that eight in ten Growth Fund borrowers (79 per cent) were in the two lowest income quintiles. Looking at Growth Fund applicants as a whole (successful and unsuccessful), 77 per cent were not in paid work. Two-thirds of applicants (67 per cent) reported net banded household incomes less than £300 per week; 15 per cent of applicants had household incomes less than £100 per week. One in five applicants (20 per cent) did not have a current or basic bank account. The survey also found that Growth Fund lenders were primarily serving a completely new market: only four per cent of applicants said they were already a credit union member or CDFI customer at the time of their Growth Fund loan application.

8.2 Growth Fund borrowers

8.2.1 Propensity to use high-cost or illegal credit

The survey data indicated that Growth Fund borrowers continued to use other forms of borrowing as well as the Growth Fund, although some of the most common types of borrowing they used did not incur interest charges. There was some suggestion, based on respondents' subjective views, that the Growth Fund had encouraged borrowers to borrow less from other sources.

Half of Growth Fund borrowers had some other form of borrowing at the time they were interviewed. The types of borrowing most often mentioned were loans from the Social Fund, loans from friends or family members where no interest was charged, home credit loans and goods bought in instalments from a mail order catalogue. Just over one in ten Growth Fund borrowers (14 per cent) said they had taken out a loan *after* their Growth Fund loan.

Growth Fund borrowers were asked if they had changed their borrowing behaviour since first starting to borrow from a Growth Fund lender. A third (32 per cent) considered that they had borrowed less from any other source since first taking out a loan with a Growth Fund lender. Almost all of these borrowers (87 per cent) attributed this change in behaviour directly to their contact with a Growth Fund lender. There was evidence that the Growth Fund had disrupted the role of high-cost credit in borrowers' lives, with around one in ten of all borrowers (12 per cent) reporting that they had used home credit less since first contacting a Growth Fund lender. A similar number of borrowers (13 per cent) reported using the Social Fund less.

8.2.2 Access to and use of appropriate financial services

An additional benefit to Growth Fund applicants, whether successful or unsuccessful, is the opportunity to access other financial services through a Growth Fund lender. The survey data indicated that the Growth Fund had resulted in the take-up of bank accounts and encouraged saving among a significant minority of applicants.

8.2.2.1 Banking

Two in five Growth Fund applicants in the survey (40 per cent) had used a Growth Fund lender that offered access to bank accounts. The remainder did not have access to a bank account in this way. Overall, 13 per cent of all Growth Fund applicants with a bank account had this account as a result of their contact with a Growth Fund lender (equivalent to 10 per cent of all applicants). This figure was higher among successful Growth Fund applicants than unsuccessful applicants. Growth Fund applicants (successful and unsuccessful) who had a transaction bank account generally seemed to make use of it, whether or not it had been opened with a Growth Fund lender.

8.2.2.2 Saving

The majority of Growth Fund applicants (84 per cent) had access to a savings account through their Growth Fund lender. The evaluation indicated that the Growth Fund lenders had some success in terms of encouraging applicants to save, despite their low household incomes, particularly through the use of 'soft compulsion' to encourage saving at the point of lending. As a result of the Growth Fund, three in ten applicants (29 per cent) now had savings in a savings account, whereas they previously had none. In addition, a third of all Growth Fund applicants in the survey (33 per cent) reported that they were actively saving into an account with their Growth Fund lender. That said, there remained six in ten applicants (60 per cent) who reported having no money saved at all, even though they were very likely to have used a Growth Fund lender that offered access to savings accounts.

8.2.2.3 Advice on money matters

The majority of Growth Fund applicants (84 per cent) reported that they had not been offered any advice on money matters (such as debt advice) by their Growth Fund lender. And, in the instances where advice was offered to applicants, it was more likely to be turned down than taken up.

When asked their subjective views about changes to aspects of money management since they first started using the Growth Fund lender, however, 39 per cent of successful applicants felt their money management skills were better. Similar proportions said they felt more in control of their finances (41 per cent); more financially secure (39 per cent) and less worried about money generally (37 per cent).

8.3 Growth Fund lenders

8.3.1 Customer profile

The impact assessment shows that Growth Fund lenders provide loans only to those that would otherwise have been able to obtain credit from the private sector, but at higher cost, rather than those for whom the credit market has failed and cannot obtain borrowing at any cost (at least through legitimate means).

The survey data indicate that the main beneficiaries of the Growth Fund have been women, people aged under 40, families with children (and single parents in particular), and people not in work. One of the main benefits of the Growth Fund from the lenders' perspective was that it enabled them to lend to financially excluded people they had not previously served, and in far greater numbers. As a result, most Growth Fund lenders in the telephone survey agreed that the customer profile of their organisation had changed significantly as a result of delivering the Growth Fund. Several of the lenders we interviewed in depth mentioned that they were now reaching far more young people than had previously been the case.

Growth Fund lenders were asked how likely they were to continue lending to the financially excluded people they had reached through the Growth Fund, when government funding ended in 2011. The response was largely positive, with almost all the lenders (75 of the 82 interviewed) reporting that they were very or fairly likely to continue lending to financially excluded people. These lenders generally considered that their volume of lending to financially excluded people would stay about the same or increase after 2011.

For the small number of lenders who said they were *unlikely* to continue lending to financially excluded people after 2011 (seven of the 82 surveyed), the main issue was resources – their organisations would simply not be able to cover the costs of lending to financially excluded people once the Growth Fund had ended. Presumably, these lenders also felt it unlikely that they would be able to access funding elsewhere in order to continue serving financially excluded people in the same way

8.3.2 Lending practices

From an organisational perspective, eight in ten Growth Fund lenders in the telephone survey reported that their organisation had improved its working practices as a result of the Growth Fund and now operated in a more business-like way.

Growth Fund lenders used a combination of methods to reach a decision about whether or not to grant a Growth Fund loan, including loan application forms, interviews with loan officers and credit checks. Factors such as the purpose of the loan and the applicant's honesty in providing the required information were taken into account when making a loan decision. Once borrowers' had established a credit

history with a Growth Fund lender, the application process for repeat loans tended to be lighter-touch.

Eight in ten Growth Fund lenders (68 of the 82 interviewed) had a dedicated credit controller on their staff. Nine in ten of them (72 of the 82 interviewed) monitored missed loan repayments at least weekly, and often daily. For the most part, the debt recovery process operated by the lender was triggered when one or two loan repayments had been missed.

8.3.3 Levels of business and capacity

In the evaluation, levels of business was assessed through volume of lending; capacity was measured by levels of paid staff and the number of service points from which Growth Fund lenders operated. While these changes cannot be attributed solely to the Growth Fund it was clear that the Growth Fund was often a driving force for change. Equivalent growth was not evident among the comparison group of third sector lenders.

8.3.3.1 Impact on volume of lending

The data provided by Growth Fund lenders in the telephone survey indicate that there was a more than 200 per cent increase in the average volume of personal loans (Growth Fund and non-Growth Fund) between 2004 (before the Growth Fund initiative)_and 2009, from 251 loans on average in 2004 to 773 loans in 2009. The average (median) total value of personal loans also increased in each of these years, from £159,032 in 2004, to £217,729 in 2006 and £411,000 in 2009.

8.3.3.2 Impact on number of paid staff and service points

On average, Growth Fund lenders employed more paid staff and increased the number of service points in both 2006 and 2009, once the Growth Fund got underway. The average (median) number of paid staff increased from 1.5 FTE in 2004, to 2.0 in 2006 and 4.0 in 2009. The average (median) number of service points increased from four in 2004, to six in 2006 and eight in 2009. In terms of increasing an organisation's capacity more generally, the lenders interviewed in depth often felt these changes heralded positive benefits for their wider membership or customer base as well.

The data provided by non-Growth Fund third sector lenders show that these lenders were in a fairly similar position to Growth Fund lenders in 2004 in terms of average (median) numbers of paid staff and service points. In contrast to the Growth Fund lenders, however, their position remained fairly static over the next five years.

8.3.4 Use of other streams of funding

Six in ten Growth Fund lenders (53 of the 82 lenders interviewed) depended on grant funding to operate. Although these lenders generally considered it likely that their organisation would become self-financing in the future, most felt that it was at least two or three years away. In addition, the main thing required for them to become self-financing was generally reported to be an injection of resources. In other words, in most cases these lenders seemed unlikely to become self-financing if they simply continued to conduct business as they currently were.

From Growth Fund lenders' perspective, the main potential for external funding in the future was seen to come from local authorities, which were already important funders for some of the Growth Fund lenders in the survey. The likely impact of public sector cutbacks in this respect was widely acknowledged, however. There was little enthusiasm among Growth Fund lenders for the idea of accessing funding on commercial terms. There was also little appetite among Growth Fund credit unions for the idea of lending above the current two per cent per month interest rate cap, if they were legally allowed to do so.

Analysis of the costs and benefits of delivering the Growth Fund indicated that higher interest rates than the 26.8 per cent charged by most Growth Fund lenders would be needed to put Growth Fund lending on a more stable commercial platform. It is estimated that, based on average operating costs since 2006, an APR of 71.2 per cent would be required to cover operational costs and financial risks associated with Growth Fund lending in its current form. Based on 2010 average operating costs, the required APR is estimated to be 39.6 per cent to break even at a cost of £60 per loan, and 48.1 per cent to break even at a cost of £75 per loan.

8.4 The costs and benefits of the Growth Fund

The cost of the administering the Growth Fund totalled £40.8m, with the additional social cost of lending (i.e. the opportunity cost of lending to borrowers) estimated at £14.3m.

The Growth Fund also displaced the profits of commercial lenders (including high cost lenders as well other credit providers). Taking into account the evidence that one of the effects of the Growth Fund was to help borrowers repay their debts over a shorter period, the estimated profits displaced are estimated to total between £21.3m to £30.5m.

The Growth Fund was found to have reduced the interest paid by Growth Fund borrowers on their lending by reducing the interest rate paid on borrowing and shortening the period over which borrowers repay their debts. Total interest savings are estimated at between £377 and £425 per borrower. Based on the 318,000 Growth Fund loans made to the end of September 2010, this means that total interest savings of between £119.1million and £135.1million were available to individuals and households in the local communities served by the Growth Fund, of which between £41.3m and £48.9m represented interest rate savings.

The Growth Fund was mainly accessed by those in lower income groups, implying a further distributional effect (on the basis that lower income groups place a higher value on additional income than higher income groups). This is estimated at between £89.9m and £101.3m if the total financial saving is treated as a benefit and between £31.0m and £36.7m if only the savings due to interest rate reductions are treated as a benefit.