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Department of Families, Housing,
Community Services and Indigenous Affairs



Community Development Financial Institutions Pilot Evaluation

Report

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Westwood Spice

*On behalf of the Department of Families, Housing, Community Services and
Indigenous Affairs*

February 2013



a strong and fair society for *all* Australians

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Westwood Spice is a specialist consulting group working with NGOs and government departments, individuals and communities to make a difference in the lives of disadvantaged Australians. Our passion is for ideas and programs that achieve positive impacts for the 'clients of our clients'.

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List of Acronyms

AAPR	Average Annualised Percentage Rate
ABA	Australian Bankers Association
ABCUL	Association of British Credit Unions
ABS	Australian Bureau of Statistics
AFIN	Australian Financial Inclusion Network
ANZ	Australia New Zealand Bank
APPG	All Party Parliamentary Group (UK Parliament)
APR	Annualised Percentage Rate
ASIC	Australian Securities and Investment Commission
ASPI	Australian Strategic Policy Institute
ATM	Automatic Teller Machine
ATO	Australian Tax Office
CCF	Community Credit Foundation
CDEP	Community Development Employment Project
CDFA	Community Development Finance Association
CDFI	Community Development Financial Institution
CFLT	Consumer and Financial Literacy Taskforce
CRA	Community Reinvestment Act
CSB	Community Sector Banking
CSI	Centre for Social Impact
CSR	Corporate Social Responsibility
DGR	Deductible Gift Recipients
DWP	Department of Work and Pensions UK Government
FaHCSIA	Department of Families, Housing, Community Services & Indigenous Affairs
FCCC	Fitzroy & Carlton Credit Cooperative
FFA	Fair Finance Australia
FLF	Fair Loans Foundation
FMP	Financial Management Program

GSM	Good Shepherd Microfinance
IBA	Indigenous Business Australia
ICAS	Indigenous Capital Assistance Scheme
NAB	National Australia Bank
NCCP	National Consumer Credit Protection
NEIS	New Enterprise Incentive Scheme
NFP	Not-for-profit
NGO	Non-Government Organisation
NILS	No Interest Loans Scheme
NFSF	National Financial Services Federation
SBB	Social benefit bonds
SEDIF	Social Enterprise Development and Investment Fund
SEFA	Social Enterprise Finance Australia
SROI	Social return on investment
SVA	Social Ventures Australia
WWS	WestWood Spice

1. Executive Summary

Introduction

The Community Development Financial Institution (CDFI) pilot was established by the Australian Government as part of a wider package of measures initiated in 2009 to build financial resilience and wellbeing among those most at risk of financial and social exclusion. The CDFI pilot is one element of the Financial Management Program, operated by the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA). As well as providing crisis assistance measures such as Emergency Relief, the Financial Management Program also aims to actively build capacity and lead to long-term financial inclusion.

In Australia, the community finance sector is under-developed compared with other countries such as the United Kingdom (UK) and United States (US). In order to explore the potential of a CDFI sector in Australia five emerging community finance organisations were provided with \$6 million in seed funding to develop the necessary infrastructure to offer financial products and services to financially excluded individuals and families. The five pilot organisations were initially funded for a 12 month period from March 2011 to March 2012. The pilot was extended in late February and it was completed on 30 June 2012.

The five pilot organisations were:

- Community Sector Banking (operating as 'In-roads');
- Fair Loans Foundation (Fair Loans);
- Foresters Community Finance (operating as 'Fair Finance');
- Fitzroy & Carlton Community Credit Cooperative (established the 'Community Credit Foundation'); and
- Many Rivers Microfinance (Many Rivers).

In June 2011, WestWood Spice was contracted to undertake an independent evaluation of the effectiveness of the CDFI pilot.

The objective of the evaluation was to assess the extent to which the objectives of the pilot were achieved with particular reference to three key evaluation questions:

- How effective were the CDFIs in increasing the ability of disadvantaged individuals to gain access to appropriate credit?
- Was the demand for appropriate financial products and services best met by CDFIs?
- What mechanisms and barriers did the CDFIs face in gaining access to capital?

The evaluation draws on data collected through quarterly performance reports, surveys of clients, workshops and interviews with CDFIs, investors and key not-for-profit organisations and a review of Australian and international literature.

Ethics approval was obtained from the Human Research Ethics Committee of the University of New South Wales.

Evaluation Findings

How effective were the CDFIs in increasing the ability of disadvantaged individuals to gain access to appropriate credit?

Despite the short timeframe of the CDFI pilot,¹ four of the five pilot organisations were effective at creating products that were attractive to people who otherwise would face financial exclusion. These included personal loans in the range of \$1,000-\$4,000 for terms of 12 months to two years. Loans could be used for a variety of purposes including purchasing household items and cars, making car repairs, paying medical expenses, consolidating debt and, for one of the CDFIs (Fair Loans Foundation), paying household bills. One of the organisations, Many Rivers, focused exclusively on microenterprise development and lending.

In addition to the provision of credit, a key component of the pilot was client support in the form of financial education, budgeting advice or money mentoring. This support proved to be of benefit to greater numbers of people than just those who secured loans. “It is not about loans” was emphasised by providers, however, previous research has highlighted the importance of loan provision, finding that access to a financial product, supported by a relationship based approach, can be important in encouraging financial participation and behaviour change (Proske 2010).

For three of the organisations, Many Rivers, Fair Finance and In-roads, financial support took the form of intensive one-on-one work with, at times, very disadvantaged clients. For these CDFIs, a key outcome of the pilot was to provide individuals with a detailed understanding of their financial circumstances. This support proved to be a major strength of the pilot program, but also its greatest cost.

Across the participating CDFIs, there was a total loan book value of \$2,827,628 at the end of the pilot. This comprised 1,053 personal loans totalling \$2,159,083 and 122 microenterprise loans totalling \$668,545 and supporting 144 businesses.²

A total of 1,093 people accessed financial literacy support or money mentoring and 367 people accessed business planning support.

At the end of the pilot, the majority of clients were on track to repay their loans and none of the pilot organisations reported concerns with the current level of arrears.

The pilot organisations also appeared to be effective at targeting individuals who were financially excluded. Results from the client survey indicated that borrowers were excluded from mainstream credit providers primarily because of low incomes or poor credit history. In terms of client demographics, almost 30 per cent of borrowers across the CDFIs identified as Aboriginal or Torres Strait Islander. This proportion was highest for In-roads (64 per cent) and lowest for Fair Finance (8 per cent). A third more women than men took out personal loans, however, more men than women received enterprise support through Many Rivers. Over a third of Fair Finance and In-roads’ clients identified as having a disability. Fair Loans was the only organisation to have a majority of clients with wages rather than government payments as their primary source of income (65 per cent).

¹ International research suggests that it can take up to five years to establish a CDFI (Jones & Ellison 2011).

² Not all businesses needed financial support in the form of a loan.

Two of the CDFIs (In-roads and Fair Loans) required individual borrowers to meet certain criteria, including earning less than \$50,000 per annum. This may have excluded some applicants, in particular people described as “working poor” earning slightly over the threshold amounts. It also created loan criteria similar to those of the StepUP product, which attracts a lower interest rate.

Feedback from the survey and interviews with clients and CDFI staff indicated increases in confidence and self-esteem attributed to having been deemed credit worthy and successfully making loan repayments.

Feedback from borrowers has underscored the positive difference which access to a small amount of affordable credit can make in the life of someone who is not included in the financial mainstream. Cementing and expanding these benefits is the challenge for the future.

Is the demand for appropriate financial products and services best met by CDFIs?

People on low incomes and those with poor credit history currently have very limited options if they require additional funds (Banks et al 2012). A CDFI is just one avenue to address the issue of financial exclusion. It is not able to meet demand for very small loans, such as people who want \$50 for a couple of weeks, or where income is inadequate for day to day expenses.

CDFIs act in the interest of clients, recommending alternatives to loans where more appropriate, and any profit generated is used as social investment to benefit the community. This is very different from the commercial situation where the key driver is the profit generated for the organisation and its owners or shareholders.

Pilot organisations were all able to supply examples of where services such as budget advice or debt renegotiation had been supplied to borrowers, and for all of the organisations (except Fair Loans) people the CDFI did not lend money to also access such services.

The CDFI relationship-based models adopted by Many Rivers, Fair Finance and In-roads partners worked one-on-one with very disadvantaged clients and helped them to establish businesses or resolve financial problems. “It is not about loans” was emphasised by providers, however, access to a financial product, supported by a relationship-based approach can encourage financial participation and behaviour change (Proske 2010). There is early evidence that the approach is gaining traction, most notably in Aboriginal communities when introduced by trusted workers, across three different pilot models. It is significant that a CDFI loan is not “charity” and offers people the opportunity to be self-reliant, grow in self-esteem and have the potential to transition to the mainstream.

Web-based products have the potential to achieve scale and to reach much larger numbers of people who may be unable to access a face-to-face service, but they are very different in impact. Fair Loans was the only organisation to have a majority of clients with wages rather than government payments as their primary source of income. The Fair Loans model was good at solving short-term funding problems but phone and email contact with the money mentor may not be as effective in encouraging longer-term behaviour change.

It is important to build scale so that individual lenders can achieve economies and so that there is wider awareness of what a CDFI offers. The UK experience suggests this will take time. Nevertheless, CDFIs can play a key role in addressing financial exclusion as part of a multi-faceted approach including subsidised no-interest products (NILS) and licensed short-term, high-interest options.

What are the mechanisms and barriers CDFIs faced in gaining access to capital?

The CDFI pilot was established on the principle that funding would be provided by the Government for business development purposes. It was a condition of the pilot that Government funds would not be used for the purpose of providing loan capital.

To assist the pilot organisations to gain access to an external source of capital, FaHCSIA facilitated an 'investment circle', made up of the four major banks, prior to the start of the pilot. The role of the investment circle was to independently assess, and invest in, potential pilot organisations from their own investment perspectives. For four of the five CDFIs a successful partnership with a bank was established, although these partnerships were not necessarily facilitated through the investment circle.³ As a credit union, Fitzroy & Carlton Community Credit Cooperative was to provide its own capital, supplemented by funding provided by other credit unions, to the newly established Community Credit Foundation.

Over \$3 million in capital funding was accessed. The Community Credit Foundation was the only CDFI that faced major difficulty securing loan capital for lending. Both Fair Finance and Community Sector Banking experienced delays early on in the pilot negotiating a quick release of funds from their commercial investors, resulting in substantial delays to their ability to lend. With the exception of Fair Loans, the capital provided has been adequate to meet client loan requirements.

For the National Australia Bank (NAB), participation in the pilot fell under a Corporate Social Responsibility (CSR) arrangement, whereby the investor provided the CDFI with a limited interest free overdraft for the duration of the pilot. NAB provided a million dollars each to both Fair Loans and Fair Finance. These arrangements enabled the CDFIs to recycle funds as they were repaid by borrowers at no additional cost to the CDFI. Many Rivers' relationship with Westpac is different, where the bank provided the business loan to the Many Rivers client. Bendigo Bank provides a million dollars allocated for In-roads lending from its balance sheet, with CSB reserving \$200,000 to take first loss risk.

At least two of the CDFIs spent a considerable amount of time seeking Deductible Gift Recipient (DGR) status in order to generate donations for their organisation. At this stage, there appears to be little appetite either from investors or from the CDFIs themselves, for exploring social impact investment⁴ as a means of securing funding. This may present a risk to the emerging CDFI sector if there is too much reliance on a single source of funding, such as through the CSR operations of the major banks. There is also evidence that the Many Rivers model, with a focus on individual enterprise and client support is more attractive to funders, and they have been successful in securing longer-term commitments from their backers.

Other issues

Delays

There was considerable variability in the start-up timeframes of each of the CDFIs. This was influenced largely by the complexity of the models being established. However, the need for the organisations to gain formal approvals for lending procedures and to establish documentation, as well as difficulties in securing loan capital, also led to substantial delays. Two of the CDFIs, Many

³ The investment circle was only one possible source of capital funding for CDFI applicants. What was important was the overall financial viability of the CDFI.

⁴ Impact investment refers to the use of financing mechanisms which delivers both financial, albeit reduced, and social returns.

Rivers and Fair Loans, were expanding pre-existing activities and were able to commence lending at the beginning of the pilot. As a result, these two CDFIs met performance targets established at the start of the pilot. Two of the CDFIs, Fair Finance and In-roads, started lending in September 2011 and were not able to achieve target loan numbers. The Community Credit Foundation was unable to commence lending.

Financial Sustainability

Another significant issue that emerged from the pilot was the ability of CDFIs to achieve financial sustainability. An original premise of the pilot was that the operational costs of CDFIs would eventually be covered by the income generated from a capital pool plus interest on loans. Although it is early days, this appears to be unsubstantiated. A number of factors were found to influence financial sustainability, including:

1. Cost of delivering services. Evidence from the CDFI sector in the US and UK, as well as other Australian microfinance initiatives, demonstrates that services for financially excluded populations are expensive to deliver. The current pilot confirmed that covering the costs of the intensive face-to-face work necessary to build financial capability can be far more expensive than the costs of simply delivering a loan. Overseas experience suggests efficiencies may be achieved if CDFIs develop other financial products such as enterprise loans or micro-insurance. Over the course of the pilot, Foresters has been able to develop its portfolio of community finance products, including a small business loans product and no interest loans for arts practitioners. In addition, Foresters was selected by the Australian Government to establish and manage two funds to support social enterprises under the Social Enterprise Development and Investment Fund (SEDIF) program.
2. Fulfilling social purpose. The amount of time spent with clients who did not receive a loan was identified as a significant cost by most of the CDFIs in the pilot. This highlights the challenge of balancing the CDFI's commitment to social purpose with the ability to remain sustainable as an organisation. In the UK, recommendations have been made to increase the sustainability of CDFIs by minimising the time spent with applicants (Dayson 2008; GHK 2010; DWP 2012). However, this may be counterproductive if the long-term goal is client financial inclusion and capacity building.
3. Scale of operations. In an Australian context, it is hard to imagine a CDFI reaching the scale required for sustainability with a sole focus on personal lending. This may be achieved with a web-based product, however, the trade-off is likely to be lower client support and less ability to target hard-to-reach groups.
4. Demand for products and services. An inherent challenge in the CDFI personal lending model is the constant need to find new customers. CDFIs are not long term financial providers, but try to offer pathways to financial inclusion. The 'best' customer for a CDFI is one who can stabilise their financial situation to the point where they are able to access mainstream financial products and services. Given the novelty of the CDFI sector and the low level of community awareness about alternatives to high-cost, short-term loans, more work needs to be done to promote CDFIs and their products.

Recommendations

Based on the evaluation findings, the following recommendations are made about the development of a potential CDFI sector in Australia.

- Extend the pilot for a further three years. This would allow time to conduct a more thorough analysis of the longitudinal impacts of CDFIs on financial exclusion. It would also facilitate the development of a CDFI sector in Australia.
- Broaden the scope of the pilot to include lending to social enterprises and not-for-profit organisations. This would increase the social impacts of the CDFIs and provide additional revenue for the CDFIs from the financial products developed.
- Develop tools to review the social impacts of CDFIs at both an individual and community level. This could utilise work being undertaken on social impact measurement by Access Economics and Net Balance in Australia, the Community Development Finance Association (CDFA) in the UK and Opportunity Finance Network in the US.
- Establish a peak body to represent and advocate on behalf of the CDFI sector in Australia. This could facilitate a process of certification of CDFIs, such as the development of an accreditation “kite mark” to identify ethical non-mainstream lenders.
- Explore the establishment of a CDFI fund that provides financial support to CDFIs.
- Ensure financial exclusion remains the focal point of any future investment in the sector. This can be achieved by ensuring that loan criteria do not exclude people who could benefit, in particular the working poor.
- Promote CDFI activities widely across Australia, specifically working to ensure that CDFIs are easily identifiable by consumers and distinguished from both payday lenders and financial literacy or consumer advocacy and support services.
- FaHCSIA and the CDFIs continue to monitor compliance with the *National Consumer Credit Protection Act 2009*. This includes working with the Australian Securities and Investments Commission (ASIC) to encourage CDFIs to improve utilisation of ASIC’s resources and to encourage CDFIs to facilitate identification of non-compliance with credit legislation at an early stage.

2. Introduction

2.1. CDFI Pilot

We need new approaches that go beyond immediate assistance to promote capacity and build confidence in managing money.

We need to give people not only the financial resources to participate but the opportunities and capabilities they need to build their own financial security.

We also want to make sure that people have access to safe and fair credit that is appropriate for their means and reflects their ability to repay.

Jenny Macklin MP

Minister for Families, Community Services and Indigenous Affairs

The Community Development Financial Institution (CDFI) pilot was established by the Australian Government as part of a wider package of measures initiated in 2009 to build financial resilience and wellbeing among those most at risk of financial and social exclusion. The CDFI pilot is one element of the Financial Management Program, operated by the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA). As well as providing crisis assistance measures such as Emergency Relief, the Financial Management Program also aims to actively build capacity and lead to long-term financial inclusion.

In Australia, the community finance sector is under-developed compared with other countries such as the United Kingdom (UK) and United States (US). A scoping study into CDFIs (SVA 2009), commissioned by FaHCSIA, suggested there are strong indications that growing a community finance sector may be beneficial to address trends such as:

- continuing demand on welfare advances as a result of limited alternatives;
- increasing reliance on credit cards;
- shift in focus of credit unions away from the community towards mainstream banking customers and practices; and
- strong growth in small amount, high cost “payday” lending.

The size and achievements of the CDFI sector in other developed nations, particularly the UK and US, also supported the exploration of possible sector growth in the Australian context.

In order to explore the potential of a CDFI sector in Australia, five emerging community finance organisations were provided with \$6 million in seed funding to develop the necessary infrastructure to offer financial products and services to financially excluded individuals and families. The five pilot organisations were initially funded for a 12 month period from March 2011 to March 2012. The pilot was extended in late February and was completed on 30 June 2012.

The CDFI pilot project was established to:

- increase the financial inclusion of individuals from target groups including Indigenous Australians and other vulnerable Australians;
- test and gain further evidence on the demand for financial services and products and the contribution of CDFIs in meeting this demand;
- facilitate capital and loan funding through a circle of investors; and

- contribute to the investigation of the infrastructure and legislative framework necessary to support CDFIs in Australia.

The pilot had two main funding components:

- provision of government funding for infrastructure and business development; and
- facilitation of an ‘investment circle’ of banks to provide funding for loan capital.

In addition, funding was provided to the Australian Financial Inclusion Network (AFIN), a network which meets quarterly to share information and support organisations with an interest in microfinance and financial exclusion.

The pilot organisations were funded to facilitate loans to individuals. Internationally, CDFIs also undertake significant work in lending to not-for-profit (NFP) organisations and to small and medium sized enterprises to assist business and community development and regeneration. In the US, CDFIs also play a key role in offering mortgages to assist with housing for people on low incomes; however, these areas are not the focus of the FMP program, nor the Australian CDFI pilot.

The five pilot organisations participating in the pilot are listed in Table 1. More detailed information on the pilot organisations can be found in Section 4.

Table 1: Five CDFI pilot organisations

Funded organisation (CDFI brand in italics)	Products/ Services	Location
Community Sector Banking (<i>In-roads</i>)	Microfinance loans Financial literacy training	In-roads works through partnerships with community organisations in all states and territories (with the exception of the ACT)
Fair Loans Foundation (<i>Fair Loans</i>)	Microfinance loans Money mentoring	Internet-based National coverage
Foresters Community Finance (<i>Fair Finance</i>)	Microfinance Debt counselling Referral	Local area via a shopfront in inner city Brisbane with outreach to adjoining communities and the Gold Coast
Fitzroy & Carlton Credit Cooperative (<i>Community Credit Foundation</i>)	Microfinance and financial literacy and budget services	Local area via a shopfront in Fitzroy, inner city Melbourne
Many Rivers Microfinance (<i>Many Rivers</i>)	Microenterprise loans, business planning and financial literacy	Offices are in: <ul style="list-style-type: none"> ▪ Northern NSW — Grafton ▪ Hunter Valley, NSW — Kurri Kurri ▪ Western Sydney, NSW ▪ Moree, NSW ▪ Pilbara, WA ▪ Goldfields, WA ▪ East Kimberley, WA — Kununurra ▪ Perth, WA ▪ Cairns, Qld

2.2. CDFI Pilot Evaluation

WestWood Spice was commissioned to undertake an evaluation of the CDFI pilot project.

The objective of the evaluation was to assess the extent to which the objectives of the pilot were achieved with particular reference to three key evaluation questions:

- A. How effective were the CDFIs in increasing the ability of disadvantaged individuals to gain access to appropriate credit?
- B. Was the demand for appropriate financial products and services best met by CDFIs?
- C. What mechanisms and barriers did the CDFIs face in gaining access to capital?

In addressing these questions, the approach taken by WestWood Spice used a “results based accountability framework” (RBA) developed by Mark Friedman. The framework draws attention to four areas of performance results: Quantity, Quality, Effort and Effect (Friedman 2005). Detailed questions have been developed to investigate the performance of the CDFIs (see Table 2).

Table 2: List of investigative questions

Investigative questions addressed in the report	Key evaluation question
Quantity	
▪ What types of financial products/ services have been developed? What services other than loans are offered (e.g. business planning, financial counselling)?	A
▪ How have products been distributed/ marketed?	A
▪ What was the take up by clients?	A
▪ What was the CDFI contribution in meeting demand compared with other loan products?	B
▪ What was the relative cost to government?	B
▪ How much capital funding was achieved?	C
Quality	
▪ What was the profile of clients accessing products/ services?	A
▪ How did the CDFIs engage with clients?	A
▪ What was the client view/ experience of the product?	A
▪ What was the experience of CDFIs in working with investors?	C
Effort	
▪ What factors influenced any variations in results between pilot organisations?	A
Effect	
▪ What were the outcomes for clients?	A
▪ How many people met their loan obligations?	A
▪ What were the outcomes for CDFIs?	B
▪ Was there a community level impact from CDFIs?	B
▪ Was the demand for financial products and services best met by CDFIs?	B
▪ Was the financial model sustainable?	B

2.2.1. Evaluation activities

The evaluation has involved the following main areas of work:

Literature review

The evaluation includes a review of literature relating to the three key evaluation questions:

- a discussion of financial exclusion and its impact;
- an assessment of the types of financial products available to those who are financially excluded; and
- an exploration of philanthropic and capital investment in the context of a potential CDFI sector.

Document review

CDFIs regularly reported on performance during the pilot period, using a standard tool devised by WestWood Spice and FaHCSIA. In addition, WestWood Spice collected materials that were developed by the pilot organisations. These included marketing materials, job descriptions, planning records and loan application documents.

Client surveys

Two tools were prepared to survey clients and these were approved by the Human Research Ethics Committee of the University of New South Wales. Both surveys offered an incentive to respondents in the form of entry into a draw to win one of ten vouchers. Trade promotion lottery licences were obtained for this purpose.

An initial paper survey (with an option to complete online) was distributed to all new clients between November 2011 and April 2012. Forty-two surveys were returned completed. The second survey was conducted by telephone (with an option to complete online). Interviews took about 20 minutes and provided participants with an opportunity to discuss their personal circumstances, the reason they applied for a loan and the impact of the loan. Clients were asked to volunteer to take part in the survey via a postcard distributed by the CDFI. Sixteen surveys were completed. Detailed analysis of survey responses is in Section 5.

CDFI interviews and roundtable

Each participating CDFI was interviewed face-to-face at least three times during the course of the pilot. In August 2011, WestWood Spice also facilitated a roundtable discussion with the CDFIs, to seek input to the evaluation design. Feedback from the pilot organisations indicated that they found this opportunity to discuss practice and share issues very beneficial.

Stakeholder interviews

A number of other stakeholders including representatives of funding organisations, community organisations, international CDFIs, as well as researchers were interviewed as part of the evaluation. WestWood Spice participated in AFIN meetings, including a CDFI workshop led by Ron Grzywinski, co-founder of Shorebank, America's first CDFI. These meetings provided opportunities to hear progress reports from pilot organisations and to discuss issues relevant to the sector.

The main evaluation activities linked to the investigative questions are summarised in Table 3. Data collection took place June 2011 to June 2012.

Table 3: Evaluation activities

RBA area	Activity/Evaluation questions	Lit review	Doc review	Client survey	CDFI survey/ interviews	Investor interview	Community interview	Researcher stakeholder interview
Quantity	What types of financial products/ services were developed? What services other than loans were offered (e.g. business planning, financial counselling)?		✓		✓			
	How have products been distributed/ marketed?		✓		✓			
	What was the take up by clients?		✓					
	What was the CDFI contribution in meeting demand compared with other loan products?	✓	✓		✓		✓	
	What was the relative cost to government?		✓					
	How much capital funding was achieved?		✓		✓			
Quality	What was the profile of clients accessing products/ services?		✓		✓			
	How did the CDFIs engage with clients?		✓		✓			
	What was the client view/experience of the product?			✓				
	What was the experience of CDFIs in working with investors?				✓	✓		
Effort	What factors influenced any variations in results between pilot organisations?		✓		✓	✓		
Effect	What were the outcomes for clients?							
	How many people met their loan obligations?		✓					
	What were the outcomes for CDFIs?		✓		✓			
	Was there a community level impact from CDFI?						✓	✓
	Was the demand for financial products and services best met by CDFIs?	✓					✓	✓
	Was the financial model sustainable?	✓	✓				✓	

3. Background

3.1. Financial exclusion

This section of the report describes financial exclusion, particularly as it relates to the target groups of the CDFI pilot. It first introduces and defines the concept of financial exclusion, before describing briefly what is known about who experiences financial exclusion and the factors that might contribute to such exclusion. A discussion of the possible impacts of financial exclusion follows.

3.1.1. What is financial exclusion?

At its simplest, financial exclusion is an inability to access the financial products or services a typical person would use to assist them to participate in the economic and social life of the community. Common Australian definitions of financial exclusion consider both the lack of access to products and services as well as the consequences of this lack of access, in terms of an increased vulnerability to practices such as payday lending.⁵ Recent studies by the Centre for Social Impact (Connolly, et al., 2011 and 2012), identified three financial products deemed to be essential for inclusion in a modern society such as Australia. These included access to a transaction account, a moderate amount of credit and general insurance.

These indicators of financial exclusion are not without their problems however. In Australia, for example, the requirement that all Centrelink recipients have a transaction account to receive payments means that the first criterion would not discriminate well between those who are financially disadvantaged and those who are not. It is also important to consider financial exclusion in context; a lack of general insurance may not be a useful marker of financial exclusion for young Australians who are studying, live at home or have few assets to insure.

WestWood Spice uses the broad definition proposed by Burkett & Sheehan (2009) below. This considers financial exclusion to be both a process and an outcome.

Financial Exclusion is a process whereby a person, group or organisation lacks or is denied access to affordable, appropriate and fair financial products and services, with the result that their ability to participate fully in social and economic activities is reduced, financial hardship is increased, and poverty (measured by income, debt and assets) is exacerbated.

Burkett and Sheehan use five key dimensions to further unpack financial exclusion (see Table 4). These suggest that addressing financial exclusion will require attention to both the design of affordable, appropriate and fair financial products and how people are made aware that the option to use the product is available to them.

⁵ Small amount, high cost lending, commonly referred to as 'payday loans' are discussed in more detailed in section 3.2.1 of this report.

Table 4: Dimensions of Financial Exclusion⁶

Dimension	Explanation
Availability	The needed service does not exist, or is not available in the individual's locality.
Access	Access barriers such as prejudice, credit record, language or physical access issues exist.
Awareness	Lack of awareness of fair products/inadequate marketing by financial service providers.
Appropriateness	Mismatch of products and individual needs e.g. repayment criteria, minimum amounts greater than individual's need or cultural factors (e.g. Islamic community beliefs about the charging of interest).
Affordability	Products available are unaffordable (e.g. minimum deposit requirements) or cost structures mean people with few financial resources are charged more.

In speaking particularly about credit exclusion, Social Ventures Australia (2009) proposed two groups of people who are financially excluded. The first group comprise individuals who simply cannot afford access to financial products because they have inadequate income to service the debt. These may include those who have little or no money, those who are homeless or those for whom the costs associated with the use of the products tip them into unmanageable debt. For these individuals, those described as 'marginally served,' the appropriate response is a charitable one such as emergency relief or financial counselling.

The second group of individuals are referred to as 'underserved'. These are people who could afford financial products and services but cannot gain access to them. Individuals in this group, for example, may be able to afford to repay an interest free product such as a NILS loan,⁷ while others may afford an appropriately structured and reasonably priced interest bearing product.

A small loans pilot funded by the National Australia Bank and conducted by MoneyFast provided additional insight into the characteristics of this 'underserved' group.⁸ The research found that many of the loan recipients in the pilot were able to afford to repay a moderately priced loan (average income was \$859 per fortnight⁹) but nonetheless were financially excluded from mainstream loan options due to defaults on their credit records (NAB, 2010). The researchers suggested that some of these people may not have been behaving prudently when it came to spending or saving. The researchers concluded that with support to increase their financial literacy and competency, some of these currently excluded people may be able to access mainstream credit (NAB, 2010).

⁶ Adapted from Burkett & Sheehan (2009), p. 4.

⁷ The No Interest Loan Scheme (NILS) offers loans between \$800 and \$1,200 at zero per cent interest.

⁸ The small loans pilot offered loans between \$1,000 and \$5,000 over a 12 month period.

⁹ 19 per cent were on a government benefit.

3.1.2. Extent of financial exclusion in Australia

Using the indicators developed by Connolly et al. (2011),¹⁰ a recent report, based on a sample size of over 50,000 people, found that 17.2 per cent of the adult population (or nearly 3 million adult Australians) were identified as either fully excluded (had no financial products) or severely excluded (had only one financial product) (Connolly et al., 2012). This was a slight increase on their earlier research when 15.5 per cent of the population were found to be fully or partially excluded (Connolly, et al., 2011).

Previous research (Chant Link & Associates 2004) found that 6 per cent of adults in Australia owned only a transaction product (which they described as minimum access) and that one-third of adults had less than \$10,000 in savings or investments.

3.1.3. Who experiences financial exclusion?

Research has identified that certain groups are more likely than others to experience financial exclusion. These include those who are geographically isolated, those with low levels of income, youth, Indigenous Australians and those with a disability. Table 5 summarises the key variables linked to financial exclusion in the literature.

Table 5: Factors contributing to Financial Exclusion

Factors contributing to financial exclusion	Reported by
Geographic isolation	Connolly & Hajaj (2001)
Low level of income	Connolly, Georgouras et al. (2011; 2012); Burkett & Sheehan (2009); Landvogt (2008)
Age (18-24; over 65)	Connolly, Georgouras et al. (2011); Fitzpatrick & Kingston (2008); Andrew Irving Associates (2006); Russell, Bailey et al. (2011)
Cultural and language variables, including recently arrived migrants	Connolly, Georgouras et al. (2011; 2012)
Indigenous status	Connolly, Georgouras et al. (2011; 2012)
Lack of access to internet/IT technology	Chant Link & Associates (2004)
Educational levels	Connolly, Georgouras et al. (2011)
Disability	Chant Link & Associates (2004)
Chaotic or unstable personal circumstances such as homelessness, mental illness, drug and alcohol dependence or criminal background	Social Ventures Australia (2009)
Voluntary self-exclusion	Connolly, Georgouras et al. (2011); Corrie (2011)

Connolly et al. (2011) corroborated international findings showing financial exclusion is concentrated among those who are most disadvantaged in society already. Poverty is the common factor for these groups, which include people with disabilities, the long-term unemployed and other welfare recipients, homeless people and single mothers.

¹⁰ Access to a transaction account, a moderate amount of credit and general insurance.

There is also strong evidence that these factors interact and may create cycles of disadvantage, where one factor compounds another, with multiple negative consequences (Australian Social Inclusion Board, 2011).

Low level of income

People on a low level of income are often unable to obtain financial products from the mainstream market. Factors include discrimination (Landvogt, 2008), lack of confidence in dealing with financial institutions (Prilleltensky, Nelson et al., 2001; Landvogt, 2008), and risk assessment policies and conditions attached to financial products (Vawser & Associates, 2009).

Pricing can also mean that products are unaffordable for many people on low incomes (Vawser & Associates, 2009). Connolly et al. (2012) found that the average annual cost of basic financial services in 2011 was \$1,794, and for 13 per cent of the population this would represent over 15 per cent of their annual income. There are also other costs faced by those on a low income. These could include, for example, high charges incurred for temporary overdrafts, bounced cheques and failed direct debits (Kempson, 2006) as well as an increased likelihood of experiencing these charges given their more precarious financial situation.

Age

Age seems to play a role in predisposition to financial exclusion at both ends of the age spectrum. Russell et al. (2011) reported that young people, largely because of their age, financial inexperience and, in many cases, lack of access to appropriate role models, are vulnerable to financial traps. Youth who are at risk and disengaged from school or employment and suffer family hardship are especially vulnerable.

Not surprisingly, Connolly et al. (2011) noted that among older individuals (those aged 65 and over) there was a much lower rate of usage of internet banking (20.6 per cent compared to 70.5 per cent amongst those aged 25–34 years). The study also pointed to overseas research which confirmed that older citizens are more comfortable with the use of cash, rather than electronic methods of payment (Fitzpatrick & Kingston, 2008) and are reluctant to use new methods of money management (Andrew Irving Associates, 2006). This may have implications for methods of service delivery that involve the use of the internet.

Indigenous status

Indigenous people are over represented as severely or fully-excluded consumers of financial services compared with the rest of the population, and are more reliant than other groups on non-mainstream credit, such as payday lenders (Connolly et al., 2012).

The removal of banking services from remote and rural communities is seen as particularly detrimental to Indigenous Australians (Connolly et al., 2011; McDonnell, 2003). The same authors also report that low levels of financial literacy are more prevalent among Indigenous communities, a factor linked in some studies to financial exclusion (e.g. Martin 2007).

Indigenous people also make up a disproportionate number of those who experience barriers to accessing electronic banking. There are a number of reasons for this, including poor technical literacy, lack of reliable phone or internet access, poor numeracy skills, low level of education, age and language barriers (Australian Financial Counselling and Credit Reform Association, 2010). Lack of positive family and peer role modelling around the management of money is also seen as a problem in Indigenous communities (Social Ventures Australia, 2009). Social Ventures Australia also note that

identity and credit check requirements and minimum account balance conditions may not be met by people on low incomes. This is particularly relevant for Indigenous Australians who may not even have access to a birth certificate.

Voluntary self-exclusion

Research has found that many people exclude themselves from financial services as they decide there is little point in applying for a financial product because they believe they would be refused (Corrie, 2011; Kempson & Whyley, 1999a).

Connolly et al. (2011) identify a range of other reasons for voluntary self-exclusion, including:

- religious or cultural reasons - particular note is made of Islamic law banking which forbids the charging of interest;
- a lack of need for financial services;
- indirect access to services through relatives or friends;
- a belief that mainstream financial services will discriminate against them;
- fear of loss of financial control; and
- previous negative experiences with the banking system.

Supply side variables

On the supply side, products appropriate to an individual's needs may not exist at all. Connolly et al. (2011) identify that low income consumers often seek loans for relatively small amounts, with fixed and affordable rates and a relatively short repayment period. They note that mainstream providers have largely withdrawn these products from the market, mostly because they are not as profitable as other products.

3.1.4. The impact of financial exclusion

The consequences of financial exclusion for individuals have been described by Burkett and Drew (2008) and Connolly et al. (2011) as including:

- increased vulnerability to payday lending - despite these products being least affordable to lower income groups;
- greater difficulties in accumulation of assets and savings;
- inability to cope with even small financial shocks or unexpected expenses;
- cost and security issues in managing cash flow and payments; and
- increased exposure to financial stress or hardship.

Financial inclusion is seen as increasingly important in reducing poverty. In discussing Australia's aid program for financial services for the poor, AusAID (2010) notes that:

By borrowing, saving or buying insurance, the poor can plan for their future beyond the short term. They can build up assets and invest in education and health. Financial services can help them cope in times of need and hardship. Beyond these very tangible impacts, access to financial services promotes social inclusion and builds self-confidence and empowerment.

This is no less so for Australians who experience poverty.

Arashiro (2010) explains that the vulnerability of low-income and disadvantaged groups to the consequences of a mistake in planning or a lack of knowledge can be devastating. Their weak access to financial safety nets, and the fact they are more likely to be financially excluded, mean that they can face long-lasting negative effects in a financial crisis.

Financial exclusion deepens disadvantage which escalates across individuals and families to communities (SVA 2009). Thus, communities where there are significant numbers of excluded individuals and families experience reduced capacity to make investments, build assets or improve lives, leading to a spiral of economic decline.

Given the focus of the CDFI pilot is providing access to credit, the next section focuses exclusively on credit products accessible to those who are financially excluded.

3.2. Access to Credit

People who are excluded from the mainstream have limited options for credit. A recent study highlighted the fact that many people who struggle to manage their finances perceive that they have no choice as customers (Banks, 2011). While family and friends are a first port of call (Burkett & Drew, 2009), many turn to alternative sources of credit.

Individuals who are financially excluded are not necessarily poor money managers. In fact, studies have demonstrated that people on low incomes can be very prudent financial managers and are reluctant to incur debt (Corrie, 2011; Mouy, 2010; Scutella & Sheehan, 2006). Initiatives to make credit available to otherwise excluded households have been shown to have positive social impacts, such as increased assets, mobility, access to training and improved health and self-esteem (Anderloni et al., 2008).

Kempson and Collard (2012) identified three particularly challenging situations for those who experience credit exclusion:

- one-off anticipated expenditure (e.g. Christmas, return to school);
- less predictable one-off expenditure (e.g. car repairs, washing machine replacement); and
- loss of earned income (e.g. ill health, job loss, retirement).

Individuals may also resort to credit when they are unable to meet regular weekly expenses (food, bills, rent), however, when used in this way, the costs of borrowing may worsen financial difficulty (Banks, 2011; Connolly et al., 2011).

Despite limited access to mainstream credit options there are a number of financial products and services that are available to those who experience financial exclusion. These come in three main forms:

- small amount, high cost 'payday' lending;
- initiatives funded by governments or the corporate sector and delivered by community organisations; and
- products offered by mainstream banking institutions.

3.2.1. Small-amount, high cost lending

Small-amount, high cost loans, also known as payday loans, are available through payday loan stores, pawn brokers and over the internet. In Australia, the number of non-mainstream organisations offering these types of loans is growing. The size of the market is currently estimated at \$800 million (Rolfe & Lentini, 2011).

Payday lenders offer an alternative to mainstream lenders to people seeking credit. They are willing to lend small amounts, some as low as \$50, for short periods and charge a fee. The term 'payday' relates to its origins in agreements made to repay loans with the next pay cheque of a borrower. In Australia repayments are usually made by direct debit and this first call on borrower income provides security to the lender (NAB, 2010; Banks et al, 2012). The low value of loans means that administration costs per loan are high to the lender (NAB, 2010).

An Australian study tracking the borrowing patterns of 112 people using payday lenders in three states found three quarters of the group borrowed less than \$500, and over half borrowed less than \$300 (54 per cent). Loans were mainly used to regular expenses, food, bills and rent (Banks et al, 2012).

There is debate in Australia and internationally about the costs involved in the payday lending sector. Burton (2010), for example, highlighted two main criticisms of payday lending in the UK, which are echoed in the Australian experience. These included the cost of the loan itself, particularly when the Annualised Percentage Rate (APR)¹¹ is considered, and the borrowing practices of payday lenders.

Repeat borrowing, for example, is considered to be a major problem for people on low incomes who are using payday short-term loans. King & Parrish's (2011) longitudinal study of over 11,000 payday loan borrowers in the US found that borrowers were in debt an average 212 days in their first year of payday loan use and an average of 372 days over two years. This study also found that borrowers' loans increased in size and frequency as they continued to borrow. Over 44 per cent of borrowers were unable to make a repayment on a due date and, as a result, incurred additional fees and charges from both their bank and the payday lender, adding to their financial problems. In Australia, Banks and colleagues (2012) found that over half of the study's participants had taken out more than 10 loans in the last 24 months, and many had taken out more than 20 loans.

There is also some evidence that payday loans are used by those who can least afford them. According to Consumer Action's 2008 survey, the core market for payday loans is low-income borrowers in their twenties and thirties. When borrowers were in employment, 73 per cent reported income levels below average, with 23 per cent reporting incomes of less than \$20,000 (Gillam, 2010). Banks and colleagues (2012) found 80 per cent of payday borrowers in their study received a Centrelink payment or pension, and most had experience of significant physical, psychological or emotional health problems.

¹¹ The APR refers to the effective interest rates charged to the borrower, taking one-time expenses such as opening fees into account. It is used to determine the total cost of credit for the consumer as a percentage of the total loan amount. Feedback from CDFIs during the evaluation suggested that clients did not understand the APR, and it was more important to explain the actual cost of the loan per week/ fortnight and the total cost if fully repaid on schedule.

Mainstream banking does not make small loans available for short periods unless the borrower has a credit card, and behaviour driven costs such as over limit fees and penalties can significantly increase the costs of credit card and overdraft products for people on low incomes. Ellison and colleagues (2011) found that some high cost products that allowed small, regular repayments were managed more effectively by borrowers on tight budgets than products with lower APRs but high risk of fees and penalties. Many people on low incomes or with poor credit histories have few alternatives other than the payday lenders, whilst the cost of this form of credit is high, it does have qualities valued by clients, particularly speed of decision and funding, flexibility and simplicity of the loan process (NAB, 2010; Banks, 2011; Banks et al 2012). Payday lenders argue that a loan from them is akin to taking a taxi or using hire equipment and should not be compared with the costs of something that is required every day or longer term; Consumer advocates point out that some predatory, lenders encourage long term and repeat borrowing (Banks 2012). Predatory practice is actively discouraged by the peak body for payday lenders the National Financial Services Federation (NFSF).¹²

A policy focus on the price of credit as the primary cause of problems amongst low-income credit users is misconceived. A more nuanced understanding of the balance between the cost of credit and the various risks to consumers' financial well-being and security is required.

Regulation needs to be sufficiently sensitive and flexible to address risks attached to products right across the market, including behaviour-driven costs and APRs, without stifling individuals' access to credit, or market innovation.

A market that features a multiplicity of high and low APR products allows low-income consumers to choose the product that best suits their circumstances and the risks that they face.

Recommendations made by Ellison & colleagues, 2011.

Governments in Australia have acted to regulate fringe lending, with its inclusion under the Uniform Consumer Credit Code. State governments in the ACT, NSW, Queensland and Victoria have also introduced interest rate caps of 48 per cent, although they are not consistent in approach. In NSW, for example, fees are included but in Victoria they are not. The Federal Government recently introduced legislation to further regulate small amount lending. The *Consumer Credit Legislation Amendment (Enhancements) Bill 2012* was passed by Parliament on 20 August 2012. Key measures include allowing a loan establishment fee of 20 per cent of the amount borrowed, and a maximum monthly fee of four per cent. Other measures include prohibition on refinancing to avoid debt spirals, simplification of hardship variation procedures, and a requirement for lenders to advise consumers of other options. During consultations on the draft legislation, the NFSF¹³ expressed concern in its submission ('20+4') that the proposed cap is unviable and will mean some lenders would not be able to continue small amount loans. Consumer advocates are strongly in support of interest rate caps and tighter regulation, and the creation of ethical alternatives for low income borrowers (Gillam 2010).

¹² See <<http://www.nfsf.org.au/is-microloan-right-for-you.htm>> accessed August 2012.

¹³ The NFSF represents almost 300 ASIC licensed small amount short term credit providers who arrange more than \$800 million of loans to over 500,000 consumers each year. Submission accessed at <<http://www.treasury.gov.au/~media/Treasury/Consultations%20and%20Reviews/2012/Consumer%20Credit%20and%20Corporations%20Legislation%20Amendments/Submissions/PDF/120508%20-%20National%20Financial%20Services%20Federation.ashx>> 19 August 2012.

3.2.2. Microfinance

Microfinance is defined by Burkett & Sheehan (2009) as a 'set of tools, approaches and strategies addressing the needs of people who are financially excluded'. Microfinance initiatives offer people on low incomes access to a range of financial services that they may be unable to access through mainstream institutions, including small loans, savings accounts, insurance and other financial products. Incentives to build financial capability through linked financial education are also available.

Microfinance activities to benefit people on low or no income, such as loan funds providing interest-free repayments, have been traced back to the 16th century (Seibel 2003). However, the term itself became more widely known in the 1970s in association with the work of the Grameen Bank in Bangladesh (Cabraal et al. 2006). In 1976, Nobel prize winner Muhammad Yunus started to make very small loans to 42 borrowers, enabling them to set up small businesses and provide incomes for their families.¹⁴ The bank now services over 8 million families with loans, savings and other products.

The microfinance approach to community development takes many different forms around the world. Cabraal (2010) found that while there is extensive literature evaluating programs in developing countries, there is much less research into their impact in developed countries.

Examples of Australian microfinance loan products aimed at those who are financially excluded include the No Interest Loans Scheme (NILS), StepUP loans, Progress Loans and Advance Loans (the latter two are no longer available). These microfinance schemes build financial inclusion through access to funds either not available through mainstream financial services, or only through high-risk products. They provide opportunities to connect with other services such as housing, welfare and health.

Program evaluations have found that as well as the direct benefits from owning new items, facilitated by the loans, participants in microfinance programs report feeling valued, having improved self-confidence and strengthened financial knowledge (Corrie 2011). Repaying a loan requires personal commitment and responsibility, in addition to sufficient disposable income. For some people this can be a new and challenging experience.

Research indicates that many people on low incomes are attracted to community-based financial services rather than mainstream providers, responding positively to personal service and showing commitment in repaying loans (Collard & Kempson 2005; Jones & Ellison 2011).

Loan repayment performance has been noteworthy. NILS, the largest program, reported a loan default rate of less than 5 per cent in 2011 across over 12,000 loans;¹⁵ the StepUP default rate was 4 per cent across 599 people; the Progress Loan program was 1 per cent across 531 people; and the Advance Personal Loan program was 2 per cent for 170 loans (Burkett & Sheehan 2009). These loan products are described in the following sections.

Research has continually confirmed the importance of the human touch and flexible, accessible services for those on low incomes.

(Jones & Ellison 2011 p. 89)

¹⁴ <<http://www.grameen.org.au/history/>> accessed 25 May 2012.

¹⁵ <<http://www.goodshepherdmicrofinance.org.au/services/no-interest-loan-scheme-nils>> accessed 20 June 2012.

No Interest Loans Scheme (NILS) and StepUP

Good Shepherd Microfinance (GSM),¹⁶ with support from NAB and FaHCSIA, operates the No Interest Loans Scheme (NILS) and StepUP. These are registered trademarked products, which make small amount funds available to eligible people on low incomes to purchase essential household items or to cover costs during chronic illness.

NILS loans are generally between \$800 and \$2,000 over a term of 12 to 18 months and are provided free of interest and fees. Loans are arranged through community organisations, which are accredited and coordinated by Good Shepherd. There is a network of over 400 NILS providers nationwide. NAB has supported the program with loan capital totalling \$23 million since 2003 (Connolly et al. 2011). In 2009 and 2011, the Australian Government provided funding to expand the NILS footprint. Total government funding for these initiatives is \$36.4 million, with provision in the budgets 2009-10 to 2013-14.

In 2011, 12,415 NILS loans were made totalling over \$11.5 million. Twenty-five per cent of borrowers identified as Indigenous and 70 per cent of borrowers were women.¹⁷ The main loan purposes between 2007-2010 were for fridges, freezers, washing machines and other household appliances (60 per cent of all NILS loans).¹⁸ A total of 2,646 fridges or freezers and 2,093 washing machines were purchased in 2010.

StepUP loans are between \$800-\$3,000 and have repayment terms of up to three years, with a low fixed interest rate and no fees. The product is offered in 32 locations across Australia and, by building a credit record, is designed to assist clients to transition from a NILS product to mainstream banking. Over 1,000 StepUP loans were approved in 2010 (Corrie 2011). The most common loan purposes are vehicles (39 per cent) and household items (26 per cent).¹⁹

Both loans also aim to assist borrowers with saving and budgeting skills.

While NILS and StepUP are very successful at addressing some aspects of financial exclusion, they also have substantial limitations. NILS and StepUP both have restricted eligibility criteria (borrowers must have a health care card) and there is limited coverage across Australia. Loans typically take a long time to approve and can only be used for very specific asset building purposes. Together, these factors mean that there remains considerable unmet demand for this type of credit product (Treasury Discussion Paper, 2012).

Advance & Progress loans (discontinued)

Between 2003-2005, Community Sector Banking (CSB) partnered with the Brotherhood of St Laurence to offer a loan product \$500-\$2,000. At the end of the two and a half year pilot, 170 loans had been made totalling \$193,749. There was only one default due to the death of the borrower and one transfer to NILS when the client's house burnt down (Scutella & Sheehan 2006). At the end of the pilot in 2006, the Brotherhood partnered with ANZ to offer Progress loans.

¹⁶ Formerly Good Shepherd Youth and Family Services. Good Shepherd Microfinance (GSM) was created in 2012 to consolidate the organisation's microfinance initiatives.

¹⁷ <<http://www.goodshepherdmicrofinance.org.au/services/no-interest-loan-scheme-nils>> accessed 20 June 2012.

¹⁸ Information provided by FaHCSIA, 7 February 2012.

¹⁹ Data from 2009 provided by FaHCSIA, 7 February 2012.

Between 2006 and 2012, the ANZ Bank supported a low-interest product developed with the Brotherhood of St Laurence. The Progress Loans program was established to explore the viability of small loans for people on low incomes. Loans of \$500 to \$3,000 were offered for household goods, or a maximum of \$5,000 for a car. During the life of the scheme, over 1,250 loans were written. The program has recently been discontinued. The Brotherhood of St Laurence's website states that:

One of the primary objectives was for the Progress Loan to be financially sustainable over time. Progress Loans has been successful in providing small loans to over 1250 people but it has been found that the program is not financially sustainable without substantial and ongoing subsidy which has been provided by ANZ.²⁰

Credit cards

When available, credit cards offered by mainstream financial institutions can provide a source of short-term credit for smaller amounts. Credit cards allow purchases to be made when a need arises, with repayments made as funds become available. The cost of owning a credit card, however, can be prohibitively high for people on low incomes. Connolly, et al., (2012) calculated an average annual cost of just under \$800 with fees and charges added.

While many people who are financially excluded are unable to access credit cards, Singh et al. (2005) suggest that 'the poor, like others in Australia, use credit cards as their first preference to access credit. This is because of their immediacy and recognition'. At the same time, Singh et al. highlight the significant disadvantages of credit cards in terms of behaviour driven costs, low minimum repayments and ease of over-commitment. They reported that 28 per cent of the poorest one-fifth of Australian households (according to net worth) has credit card debt with a median value of \$2,000.

Credit card debt was the largest contributing factor for the 1,030 people seeking support from the financial counselling services of Good Shepherd in 2009-10 (Webster, 2010). Problems may be caused by high credit limits, with people accumulating more debt than they are able to repay, high fees and compounding interest incurred if they are unable to pay off the full amount owing each month. Corrie (2011) found that many people on low incomes preferred to use debit cards so that they only spent money they had already saved. Interest-free periods on store cards provided an alternative for those able to meet the loan repayment requirements and satisfy the store card conditions relating to their credit history.

There is also some evidence, however, that low-income earners manage credit cards at least as well as higher income earners. Data from Visa International (Singh et al., 2005) suggest:

Low-income earners (\$15,000 p.a. or less) represent only 5 per cent of cardholders and account for only 4 per cent of interest bearing card debt. This group pays off their card bills in full by the due date in the same proportion as do many higher income earners ...

²⁰ <<http://www.bsl.org.au/progressloan>>.accessed 21 May 2012.

3.3. The role of CDFIs in addressing financial exclusion

CDFIs are independent financial institutions that are defined by two characteristics:

- social purpose — serving those who have difficulty accessing mainstream financial services; and
- a business model that maximises financial sustainability leveraging government, philanthropic and private investment to cover costs and even generates a return on capital investment.

The debate, both in the literature and in practice, has centred on the balance between these two characteristics.

CDFIs are challenged by the degree to which financial sustainability can be achieved while focussing on people or enterprises and organisations deemed ‘unbankable’ or unviable (too risky or expensive) for mainstream organisations to service (GHK 2010; Glouvkoviezoff 2011; Jones 2011). Distinctively, CDFIs operate according to a double bottom line, addressing financial disadvantage while aiming to be self-sustaining, raising income through philanthropic and yield-based investments rather than relying on money from government (GHK 2010).

The CDFA definition:

CDFIs lend money to businesses, social enterprises and individuals who struggle to get finance from high street banks and loan companies. They help deprived communities by offering loans and support at an affordable rate to people who cannot access credit elsewhere.

www.cdfa.org.uk accessed 25 June 2012

3.3.1. US experience

CDFIs operate in low-income communities across the US. There are an estimated 1,295 CDFIs operating in the US, with around 800 of these registered to access funding and other support programs, such as through the CDFI Fund.²¹

The scale of the sector in the US is much larger than anywhere else in the world and the loan portfolio is also different. In the US, housing loans are the main activity for CDFIs and 57 per cent of funding goes to social housing (SVA 2009). This means that loans are for relatively large amounts. Default rates tend to be low, below one per cent, which contributes to sustainability (Vik 2009).

In 2008²² CDFIs across the US:

- financed and assisted businesses and micro enterprises that created or maintained 35,624 jobs;
- financed the construction or renovation of 60,205 units of affordable housing;
- provided 16,405 responsible mortgages to first-time and other homebuyers - housing finance accounted for 40 per cent of the funds lent by CDFIs in 2008; and
- provided personal loans of \$US1.3 billion (approximately 8 per cent of total funds lent).

The CDFI sector is well supported in the US, both through funding and through legislative support such as the Community Re-Investment Act (CRA). Seven per cent of CDFI capital comes from federal

²¹ The CDFI fund provided \$US 120 million dollars; the American Recovery and Stimulus Act provided \$US 100 million in additional stimulus funds to the CDFI fund in 2010 (CDFI fact sheet <<http://www.cdfi.org>> accessed 25 May 2012).

²² <http://opportunityfinance.net/store/downloads/cdp_fy2008.pdf> The CDFI Data Project is an industry collaborative that produces data about CDFIs. The most recent report is 2008 and is based on the survey responses of 495 CDFIs.

and eight per cent from state governments in the US. CDFIs also attract investment from other sources. The top four are:

- individuals — through savings and transaction accounts in community development banks and credit unions;
- banks — making funds available for relending. Incentives are available to banks through the CRA for support of CDFIs; other financial institutions (insurance companies and mutuals that are not banks); and corporations

The CDFI Fund estimates that CDFIs leverage each appropriated financial assistance dollar from the CDFI Fund with an average of \$20 in private and other non-CDFI Fund dollars. Since 1995, its first year of funding, the CDFI Fund has made more than \$1.13 billion in awards to CDFIs and financial institutions through the CDFI, BEA, and Native Initiatives Programs.²³

The CDFI sector in the United States also has a process of certification. To be eligible for certification, CDFIs need to be not-for-profit organisations with a primary mission of promoting community development through financing initiatives. At least 60 per cent of financing activity needs to be focussed on one or more specific target populations or markets. This includes underserved communities and areas falling short against socio-economic measures. CDFIs are expected to include community representation (for example, on their board) and provide services such as financial counselling or education alongside financial products.

There are six types of CDFI in the US, all of which have a different purpose and market to a different group of borrowers and investors. These are listed in Table 6.

Table 6: Types of CDFI

Types	Purpose	Borrowers	Capital Sources	Financial Products & Services Offered	Technical Assistance Provided
Community Development Bank	To provide capital to rebuild lower-income communities through targeted lending and investment	Non-profit community organisations, individual entrepreneurs, small businesses, housing developers	Deposits (often below market investments) from individuals, institutions and the government	Mortgage financing; home improvement, commercial business, non-profit and student loans; consumer banking services	Usually sub-contractors or separate subsidiaries offer credit counselling, business planning
Community Development Credit Union	To promote community ownership of assets and savings, provide affordable credit card and retail financial services to lower-income people with special outreach to minority communities, take deposits and make loans only to members	Members of the credit union (usually individuals)	Member deposits and limited non-member deposits from social investors, the government	Consumer banking services (e.g. savings accounts, check cashing, personal loans, home rehabilitation loans)	Credit counselling, business planning

²³ <http://opportunityfinance.net/store/downloads/cdp_fy2008.pdf> The CDFI Data Project is an industry collaborative that produces data about CDFIs. The most recent report is 2008 and is based on the survey responses of 495 CDFIs.

Types	Purpose	Borrowers	Capital Sources	Financial Products & Services Offered	Technical Assistance Provided
Community Development Loan Fund	To aggregate capital from individuals and institutional social investors at below-market rates and re-lend this money primarily to non-profit housing and business developers in urban and rural lower-income communities	Non-profit community organisations, social service provider facilities and small businesses	Foundations, banks, religious organisations, corporations, the government, insurance companies and individuals	Construction; pre-development; facilities and business start-up and expansion loans	Extensive guidance before, during and after the loan transaction
Community Development Venture Capital Fund	To provide equity and debt with equity features for medium-sized businesses to create jobs, entrepreneurial capacity and wealth that benefit low-income people and communities	Invests in small to medium-sized businesses in distressed communities that hold the promise of rapid growth	Foundations, corporations, individuals, the government	Commercial equity investments and loans with equity features	Extensive technical assistance to portfolio companies, including taking seats on their board of directors
Micro-enterprise Development Loan Fund	To foster social and business development through loans and technical assistance to low-income people involved in very small businesses or self-employed and unable to access conventional credit	Low-income individuals and entrepreneurs	Foundations, the government	Micro-business start-up and expansion	Substantial training and technical assistance in social and business development
Community Development Corporations	To revitalise neighbourhoods by producing affordable housing, creating jobs, and providing social services to low-income communities	Entrepreneurs, homeowners, business owners, consortia of community residents	Banks, foundations, corporations, other private support, the government	Equity Investments, mortgage lending, debt financing, linked deposits, Individual Development Accounts	Marketing, business planning, flexible manufacturing networks, business improvement

Source: Coalition of Community Development Finance Institutions²⁴

²⁴ <<http://cdfi.org/index.php?page=info-3>>, accessed 25 May 2012.

²⁵ <http://opportunityfinance.net/store/downloads/cdp_fy2008.pdf>.

3.3.2. UK experience

CDFIs in the UK have grown substantially in numbers over the past decade. From just three CDFIs in 1984 and 27 in 2000, the sector grew rapidly to peak at 80 organisations in 2006. In 2010, there were 66 CDFIs operating, with an outstanding loan portfolio of £531 million (CDFA, 2010). The reduction in numbers from 2006 is partly linked to the consolidation of CDFIs, but also to the end of the Phoenix Fund, a UK Government program that funded enterprise lending (CDFA, 2010). Proposals are currently before the UK Parliament to amend the *Financial Services Bill* to introduce a CRA-based approach requiring financial institutions to report on activities and make services available to disadvantaged communities (CDFA, 2012).

Most CDFIs in the UK are small, with 78 per cent having less than 10 staff (CDFA 2009). They provide loans and other financial services to three main markets:

- personal lending;
- business lending; and
- civil society lending (NFPs and Social Enterprises).

Table 7 highlights the proportion of loans for each market. The percentage of personal loans compared with business and civil society loans is low in value but high in number (CDFA 2010). CDFIs are reporting an increase in demand and, associated with that, increased costs in assessing applications. This table also demonstrates the importance of diversification for CDFIs in the loan market.

Table 7: Distribution of loans by number and value

Market	Loan % x number (N = 19,000 loans)	Loan % x value (Total loan value = £200m)
Personal Loan	80%	
Business Loan	17%	
Civil Society Loan	3%	

CDFIs were identified as the most important source of start-up funding for business in the UK (Dayson et al. 2011).

UK CDFI key facts:

- the average APR for a CDFI personal loan is 31 per cent, compared to 230 per cent APR in the home credit market²⁶;
- personal lending CDFIs charge an average of £17 per £100 borrowed, compared with £68 in the home credit market;
- the average loan size is £490; and
- a third of CDFI personal loans are for consumer goods, with a quarter for debt management (CDFA 2010).

The CDFA found that CDFIs providing finance and advisory services had an average default rate 3 per cent lower than those who provide finance only.
(CDFA 2009)

²⁶ Home credit in the UK is provided by agents of lenders visiting people at home to arrange loans and collect payments.

A major factor influencing payment delays and defaults is the relationship based work in the provision of advisory services. The CDFA found that CDFIs providing finance and advisory services had an average default rate 3 per cent lower than those who provide finance only (CDFA 2009). People with poor credit ratings in particular benefit from an individualised approach that provides both assistance dealing with issues and contributes to the creation of a positive credit history.

The table below summarises the cost of credit to borrowers using CDFIs. As a comparison, credit unions in the UK also lend to marginalised groups and interest is capped by legislation at 2 per cent per month on the receding balance of the loan (an APR of 26.8%).²⁷

Table 8: UK CDFI cost of credit 2009–10

	Average loan size	Interest Rate		Fees		APR	
	£	Avg %	Range %	Avg %	Range %	Avg %	Range %
Micro lending	10,077	12.3	3–32	1.5	0–10	14	2–25
Small business lending	35,500	11.5	5–18	1.5	0–5	14	9–35
Personal lending	491	26.1	10–38	2	0–5	31	14–44

Source: CDFA 2010 pp. 21 & 35

The UK CDFIs use a mixture of funding sources, generally comprising grant income plus earned income for operations and grant and investment income sources for on-lending. In 2009-10 earned income (income from lending activities) represented 40 per cent of total income raised in the sector.

3.3.3. The Australian experience

While CDFIs have a longer track record in the UK and US, Burkett (2010) notes we need to use caution when comparing them to the Australian context necessary. In both these places, the number of CDFIs has grown in the past decade supported by government funding and policy initiatives to stimulate jobs, community facilities and financial services for low income people (Parker & Lyons 2003).

CDFIs are relatively new institutions in Australia. Parker and Lyons, writing in 2003, commented that the financial dimension to community development had not been recognised in Australia and, while there were a small number of ‘proto-CDFI’ organisations, such as Maleny Credit Union, Foresters ANA Friendly Society and the Traditional Credit Union, they were underdeveloped. Parker and Lyons described Australia as “a significant exception among developed western countries” with a need to support the institutional development of CDFIs (Parker & Lyons 2003).

Foresters Community Finance (2009) highlighted the important role CDFIs have in addressing not only the financial exclusion of individuals, but of social enterprises and community organisations:

²⁷ A recent study for the Department of Work and Pensions (UK Government) recommended an increase to 3 per cent per calendar month on this cap. DWP Credit Union Expansion Project. (2012). Project Steering Committee Feasibility Study Report May 2012. <<http://www.third-sector.co.uk/wp-content/uploads/2012/05/credit-union-feasibility-study-report.pdf>>, accessed 20 June 2012.

Financial exclusion in Australia affects individuals (particularly those living on low incomes who are also asset poor); social enterprises and social businesses; and non-profit community sector organisations. CDFIs could and should play an important role in addressing the financial exclusion of all of these groups.

CDFIs must have a social purpose and aim to deliver wealth creation and asset building into communities that are most disadvantaged or underserved. They will achieve this by channelling investment into these communities; building, managing and making the best use of community-owned assets; and supporting people to access the capital needed to build their assets as a pathway out of poverty. Although they might resemble banks or investment companies, what distinguishes CDFIs in the market is their social purpose.

In Australia, Foresters Community Finance has been one of the main organisations advocating for the development of a CDFI sector. To this end, the organisation has developed a set of principles for the foundation of a CDFI sector in Australia. These capture the distinctive nature of CDFIs and the intent of their own organisation (Foresters Community Finance 2009). As can be seen from these foundational principles, the role of a CDFI is described as encompassing community sector and business lending as well as capacity building in communities. The CDFI pilot organisations have a focus limited to personal lending. The evaluation of their success will need to be seen in this context and in the wider context of experience elsewhere.

Ten Foundational Principles for Community Development Finance Institutions (CDFIs) in Australia

Context — CDFIs should be developed for the uniquely Australian context;

Focus — CDFIs should focus on addressing financial exclusion of individuals, social enterprises/businesses, and community sector organisations;

Purpose — CDFIs must have a social purpose and aim to deliver wealth creation and asset building into communities that are most disadvantaged or underserved;

Synthesis of Skills — CDFIs should synthesise the best of private, public and community sector strategies, skills and knowledge;

Sustainability — CDFIs must be structured for sustainability;

Social Impact — CDFIs must be impact focussed organisations;

Support and Capacity Building — CDFIs must build the capacity of people, businesses and organisations in the markets in which they operate;

Innovation — CDFIs should seek the leading edge of innovation in addressing financial exclusion;

Enabling Policy and Regulatory Environment — CDFIs should be supported and monitored through appropriate policy and regulation;

Source of Capital — CDFIs should be structured to enable capital and investment to be sourced from a diverse base — with the majority of their funds coming from capital markets to ensure their long-term sustainability.

3.4. Sustainability

Financial sustainability is defined as the ability of the CDFI to cover its operational costs and also meet its capital requirements through earned income.

Operational sustainability is defined as the extent to which the CDFI can cover operational costs (staffing, overheads) through income generated through its core activities (interest on loans, fees, interest earned on invested capital reserves).

(GHK 2010; Swivel 2010)

A major challenge for CDFIs is to balance financial and operational sustainability with their focus on social mission and impact. Small loans to high-risk markets and borrowers requiring support are by definition expensive (demonstrated by their exclusion from the mainstream) (NAB 2010). The experience of Advance Loans, requiring some \$100,000 in subsidy after almost three years of operation (Scutella & Sheehan 2006), and the recent closure of the Progress Loans program underscore the challenge in Australia.

In both the US and UK, the government has assisted CDFIs in line with public policy goals by making funds available to lend (the Growth Fund in the UK for example) and with infrastructure support. However, there is an underlying premise that the long-term goal should be an ability to operate without public funding (GHK 2010). Burkett (2010) highlights the different capital requirements of social enterprises at four key stages of development: start up, development, growth and maturity. She points out that unless an enterprise can cover core operating costs from operations and production from quite early in its life, then it will not be viable.

A UK study of the CDFI sector found median levels of operational sustainability at 39 per cent of CDFIs and financial sustainability at 24 per cent.

Research suggests drivers increasing the likelihood of sustainability in CDFIs and credit unions were:

- increased scale of capital to lend (achieves portfolio income and larger — more efficient — loans);
- improved partnership working/referrals;
- increased staff efficiency, broad formal and informal supports to clients;
- improved portfolio performance — reduction of bad debt and arrears and maximising use of loan fees and interest rates; and
- reduced numbers of very small loans (Dayson et al. 2008; GHK 2010; Putill et al. 2012).

Activities undertaken by CDFIs to increase operational sustainability may extend beyond lending to include back office business services to charities, training/ consultancy and management of loan funds.

However as the authors of the GHK study point out: “Inherent within the drivers of sustainability are clear trade-offs between pursuing sustainability and securing ‘depth of reach’ against policy targets” (GHK 2010). GHK identified mission creep within the sector, for example less risky clients preferred to those more challenging to serve (but higher in impact).

The GHK Consultants’ evaluation of UK CDFIs in 2010 found that the sector “remains a long way from achieving operational sustainability and even further from achieving financial sustainability” (p. iv).

One response being explored by credit unions in the UK, many of whom offer personal loan products, is to create a common 'back office' for centralised banking and credit checks for example and thus reduce transaction costs (ABCUL 2011).

Similarly, while sustainability might be possible in a developing country microfinance setting, with low labour costs, it is more challenging in developed economies. An additional pressure on sustainability is the need to invest in research, to diversify income sources, and to innovate and renew. Development services for clients such as financial literacy or budget support (a requirement of CDFI certification in the US but not generating income) are also costly to fund (Vik 2009).

A UK study of credit unions which includes a detailed breakdown of typical set up costs, suggests that between four to five years is usually required before sufficient loan interest is generated to cover operating expenses (Jones & Ellison 2011). One UK initiative by the Association of British Credit Unions (ABCUL) to reduce the costs of loans administration and create a platform for growth in the sector is a proposed central back office and electronic hub; collaboration on areas such as website development, credit administration and controlling bad debt are also viewed as opportunities (Jones & Ellison 2011).

The UK and US experience suggests that it will take some time before an Australian CDFI sector is able to be sustainable, and it will be important to be specific about the social/public policy impacts sought alongside the financial and operational sustainability of CDFIs. This experience also suggests that the scope of the target markets addressed by CDFIs may need to be broadened from their current restricted base in Australia of personal lending.

In Australia and overseas, recent research has highlighted the lack of safe alternatives for people who need credit (Banks 2011; Gibbons et al. 2011). The literature has tended to emphasise the price of short-term, high-cost credit focussing on the interest rates charged. One specific question raised by some stakeholders working for NFPs in interviews relates to the interest rates charged by CDFIs. The pilot is supported by government funding, and in some cases there appears to have been an expectation that interest would be comparable to StepUP or Progress Loans. Clients in interviews however, seem reasonably happy with interest rates charged, and are appreciative of finding organisations that will help them solve problems. It seems more important to the client that they can service the amount agreed for each payment than how much they pay overall.

The CDFA Peak Body sums up the sustainability challenge faced by CDFIs:

CDFI customers are relatively resource intensive to serve, given that many often require extensive up-front and ongoing business or financial capability support and advice. In addition, most CDFIs carry out extensive due diligence checks when vetting applicants. Therefore by definition CDFIs will rarely be in a position to meet all their capital and revenue requirements purely from all lending activity.

(CDFA 2010 p. 12)

3.5. Philanthropic and capital investment in the context of a potential CDFI sector

Many successful non-profits are constrained from expansion by difficulties in raising capital and many potentially important social innovations are strangled by their inability to raise start-up.

(Lyons 2007 p. 99)

The literature suggests that Australian NFPs and social enterprises are challenged by the lack of capital available to fund start up, development and growth (Lyons et al. 2007; Burkett 2010; Steffens 2011). CDFIs are not immune from this challenge. While some barriers to funding may be on the demand side, with boards or management reluctant to take risks and content to rely on grant funding, other barriers are linked to the supply side and the willingness of investors to provide suitable funding (Lyons et al. 2007; Burkett 2010; Steffens 2011).

Charlton (2009) suggests 'Individuals and institutions in Australia, as they are globally, are beginning to look for something that provides more than traditional investment and philanthropy' (p. 6). This section discusses what the literature tells us about types of philanthropy operating in the Australian context. This includes business giving, trusts and foundations and the emerging models of impact investment. It also considers demand-side barriers that may impact on organisations that are developing CDFIs.

3.5.1. Types of Philanthropy and levels of giving

One possible source of capital for CDFIs is philanthropy. Research into philanthropy in Australia is still embryonic (Scaife et al. 2011). Some of the difficulties in undertaking research relate to problems of definition and of differences in regulations and reporting requirements governing activities in each of the states and territories (Productivity Commission 2010).

The literature that exists has tended to focus on levels of giving, in particular comparisons in levels of philanthropy between Australia and other countries, together with some discussion of what measures are most appropriate. The Giving Australia project (2005) estimated total giving of money, goods and services by individuals and businesses at almost \$11 billion per year. Of this, \$2 billion includes funds raised through raffles and other forms of charitable events. International comparisons are difficult for similar regulatory and definitional reasons, but recent research suggests that Australians give slightly less in terms of financial donations per capita than the UK and Canada, and significantly less than the US (Effective Philanthropy 2011).

The section following discusses types of philanthropic giving and the volume of funds dispensed.

Trusts and Foundations

Philanthropy Australia estimates the total number of trusts and foundations in Australia at about 5,000, making annual donations estimated at between half a billion and one billion per annum.²⁸

²⁸ <<http://philanthropywiki.org.au/index.php/Category:Statistics>>.

A 2010 Philanthropy Australia survey of member foundations found:²⁹

- the total estimated annual giving of respondents was \$233,664,050 in grants;
- the amount given by individual foundations varies from \$10,000–\$100,000,000; and
- the average grant was \$376,877 per organisation.

The main issues identified by foundations reported in the survey were:

- the level of poverty and disadvantage in Australia today;
- the health and capacity of the not-for-profit sector;
- leveraging resources to maximise impact; and
- promoting and growing philanthropy.

Funds under management by respondents total more than \$4.75 billion. The table below highlights the disbursements made by the 10 largest trusts and foundations in the financial year 2010-2011.

Table 9: Disbursements by top 10 Australian Trusts and Foundations

Name	Disbursement (2010-2011) \$ millions
Macquarie Group Foundation	17.7
The Ian Potter Foundation	12.4
The Sidney Myer Fund and The Myer Foundation	11
Lord Mayor's Charitable Foundation	7.7
Geoffrey Gardiner Dairy Foundation	7.2
AMP Foundation	6.2
Colonial Foundation	5.6
Helen Macpherson Smith Trust	5.5
R.E. Ross Trust	5.3
The William Buckland Foundation	3.3

Source: Philanthropy Australia³⁰

There are restrictions in the areas trusts and foundations can give grants to relating to the conditions of their establishment, and this may be a barrier to CDFIs accessing such funding.

The Senate Economics Committee inquiry report, *Investing for good: the development of a capital market for the not-for-profit sector in Australia* (2011), recommended that a Social Investment Taskforce consider the potential for philanthropic trusts and foundations to invest a percentage of their corpus in social investments options (Recommendation 4.3).

Business giving

Another potential source of capital is private sector philanthropy and social investment, as part of corporate social responsibility.

In the 2003-04 financial year, total business giving was estimated by the Giving Australia report at \$3.2 billion from 525,900 businesses (67 per cent of all businesses).

²⁹ The survey of member foundations attracted ninety-six responses (44 per cent response rate). <http://philanthropywiki.org.au/index.php/Philanthropy_Australia_Member_Survey_2010_Report> include data accessed in these websites.

³⁰ <http://www.philanthropy.org.au/research/factsheets/PA_factsausfdns.pdf> accessed 20 June 2012.

Giving comprised:

- 68 per cent in financial contributions (\$2.21 billion) including:
 - donations \$1.9 billion;
 - sponsorship \$0.81 billion; and
 - community business projects \$0.64 billion;
- 16 per cent in goods (\$0.52 billion); and
- 16 per cent in services (\$0.52 billion).

Business giving can take many forms including pro bono work, employee volunteering, gifts in kind as well as grants and donations. Activities may be linked with specific benefits to the business in terms of marketing and brand positioning, for example, Ronald Macdonald Houses or Heart Foundation 'ticks' on food products, or with organisational benefits such as increased staff motivation, skills or attraction as an employer (Cavill & Company 2004).

However, CDFIs may face barriers in accessing this capital from corporations because of competition from other causes within Australia's large NFP sector.³¹

Starbucks and OFN (Opportunity Finance Network) formed the Create Jobs for USA Fund to mobilize donations from individuals, the Starbucks Foundation, and other institutions to provide capital grants to non-profit CDFIs. Starbucks is supporting the fundraising through a major national campaign in its 6,800 stores, online, in the national media, and by other means. The Create Jobs for USA Fund is housed within OFN.

The Starbucks Foundation seeded the Fund with a \$5 million donation, and the Fund grows through contributions made by individuals at U.S. Starbucks locations and online at createjobsforusa.org. Donors who contribute \$5 or more to the initiative at Starbucks locations receive an "Indivisible" campaign wristband.

<<http://www.opportunityfinance.net/financing/default.aspx?id=5742>>

The issue of business giving by banks to address financial exclusion is discussed by Howell & Wilson (2005) and Wilson (2011). They highlight the development of clear policies, including mandating bank support of initiatives to address financial exclusion. To achieve this, they advocate a regulatory response.

The New Economics Foundation in the UK found that voluntary partnerships between banks and CDFIs for funding, investment and referrals have not been established to the extent envisaged or required to develop the sector. Like Howell & Wilson they recommend performance based legislation and incentives to require cooperation (New Economics Foundation 2008).

Regulation has improved the flow of capital to CDFIs. In the US, regulations under the Community Reinvestment Act (CRA) require banks to disclose their work in their communities and thus expose financial exclusion and encourage investment.³²

³¹ The not-for-profit (NFP) sector is large and diverse, with around 600 000 organisations. The ABS has identified 59 000 economically significant NFPs, contributing \$43 billion to Australia's GDP, and 8 per cent of employment in 2006-07. The NFP sector has grown strongly with average annual growth of 7.7 per cent from 1999-2000 to 2006-07 (Productivity Commission, February 2010).

³² The CRA is intended to encourage depository institutions to help meet the credit needs of the communities in which they operate, including low- and moderate-income neighbourhoods, consistent with safe and sound operations. It was enacted by the Congress in 1977 (12 U.S.C. 2901) and is implemented by Regulation BB (12 CFR 228). The regulation was substantially revised in May 1995 and updated again in August 2005. The CRA requires that each depository institution's

In Australia, like the UK, such engagement is voluntary. Some banks in Australia have been primary supporters of CDFIs and have a number of financial initiatives to address financial exclusion. These initiatives sit within social or community affairs departments. The NAB provides support for NILS and StepUP loans and two CDFI pilot organisations (Fair Loans and Fair Finance), while the ANZ has backed Progress Loans and continues to support the Money Minded³³ program. Bendigo Bank has supported Advance Loans and through Community Sector Banking (CSB) provides the loan portfolio for the In-roads CDFI pilot. Westpac provides support for the Many Rivers CDFI pilot. Despite this, Wilson (2011) argues that voluntary corporate social responsibility initiatives will be inadequate to resolve the issue of financial exclusion.

3.5.2. Impact investing

'Impact investing' is a nascent form of philanthropy in Australia, which allows parties from a range of sectors to partner together. It has also been termed 'venture philanthropy' or 'philanthrocapitalism' (Charlton 2009; Steffens 2011).

Charlton (2009) defines the term 'impact investing' as 'profit seeking investing to generate social and environmental good'. This approach combines investing and social benefit in the context of a social financial market. In Australia the Goodstart Consortium case below illustrates this approach.

The landmark social investment so far has been the \$165 million acquisition of the ABC Learning Centres by the GoodStart consortium in 2009, which dwarfs all the other \$100,000 and small-million-dollar range in the sector.

Seeking to rescue tens of thousands of childcare places in Australia following the collapse of ABC, non-profits including Social Ventures Australia, Mission Australia and the Benevolent Society invested some of their own funds, obtained a \$15 million loan from the federal government and \$120 million in debt-financing from NAB.

The remaining \$22.5 million was raised through social capital - issuing eight-year social capital notes to private investors with a fixed interest rate of 12 percent.

(Steffens 2001)

Impact lending is still relatively new in Australia. For example, as Steffens (2011) discusses, a \$35 million charitable bond issued by the charity Chris O'Brien Lifehouse raised less than a tenth of the targeted amount.

In 2010, the Australian Government introduced the Social Enterprise Development and Investment Funds (SEDIF) with the dual aims of expanding the supply of capital available to social enterprises and building the impact investing market in Australia. \$20 million in grant funding was made available to seed the establishment of investment funds that provide loans and equity investments into social enterprises. Funds managers were required to match this capital on a one-to-one basis with private investment.

Funding was awarded to three successful funds managers:

- Foresters Community Finance was awarded \$6 million, with initial leverage from investment partner Christian Super creating a \$12 million fund.

record in helping meet the credit needs of its entire community be evaluated periodically. That record is taken into account in considering an institution's application for deposit facilities.

<http://www.federalreserve.gov/communitydev/cra_about.htm> accessed 28 May 2012.

³³ MoneyMinded is a financial education program which helps people make informed decisions about the use and management of their money. In Australia more than 125,000 people having participated in the program since 2005. <<http://www.moneyminded.com.au/>>.

- Social Enterprise Finance Australia (SEFA) received \$10 million in seed funding to establish the SEFA Loan Fund, creating a \$20 million fund with initial leverage from a range of individual and corporate investors.
- Social Ventures Australia (SVA) was allocated \$4 million in seed funding with initial leverage of \$4.6 million in private investments to establish the \$8.6 million SVA Social Impact Fund.

All funds managers are expected to attract further investment over time to grow the funds.

SEDIF funds managers take a holistic approach to assessing the investment readiness of social enterprises and offer flexible financial products based on their particular needs.

The NSW Government³⁴ is experimenting with the concept of social benefit bonds (SBBs), modelled on the UK's social impact bonds, introduced by the Cameron Coalition Government after the 2010 UK election. The bonds are financial instruments that pay a return to investors based on the achievement of agreed social outcomes. It is anticipated that the improved social outcomes will reduce demand for future government services.

In March 2012, the NSW Government announced three pilot social bonds:

- the Benevolent Society, backed by Westpac Corporation and the Commonwealth Bank of Australia, will develop a \$10 million bond to support 550 families over five years to reduce the number of days that children spend in foster care;
- a second \$10 million bond will involve UnitingCare Burnside working with children up to five years of age and their parents over a seven year period; and
- Social Finance, a Sydney-based organisation modelled on the UK social investment bank which developed the UK bonds, will work with Mission Australia on a \$7 million bond to assist 500 young adult repeat offenders for up to 6 years.

Commercial borrowing at market rates

In the UK recently, CDFI Fair Finance has been successful in obtaining market rate debt of over £3 million to fund expansion of its personal loans business. After a year and a half of unsuccessful applications for loans by Fair Finance, three banks provided £2.5 million of debt finance. An additional £750,000 of capital underwriting operating costs is provided by philanthropists. They will have funding returned in seven years with up to 5 per cent interest per annum (Social Impact Investing 2011). The approach is seen as setting a new model for CDFIs to finance growth capital:

“Ultimately, this is about leading the way toward a banking industry that is better able to serve the poor,” says Rahman. “Arranging the financing has required specialist help, legal support, advisors, and a really strong board. We’ve had to bend ears, pull favours, and find ways of keeping up morale when every door kept shutting in front of us. It has meant understanding in the most minute detail how the business worked, how we were going to scale it, and how we could find the right skills to deal with becoming a much more complex organization.” Rahman hopes Fair Finance’s success will inspire other microfinance organisations in wealthy countries to approach commercial lenders for growth capital. If more do so, they will need to balance three goals. They will need to make their loan book financially sustainable, build models to reach the poorest of the poor, and produce a positive net gain for society in economic growth or poverty reduction. Fair Finance is proof that a locally rooted, innovative, and entrepreneurial organisation can meet this triple goal through partnering with mainstream commercial lenders. (Buckland & Hay 2012)

³⁴ <<http://www.probonoaustralia.com.au/news/2012/03/nsw-govt-announces-social-bond-pilot-selection>>.

Big Society Capital

In the UK, the government has created a capital fund with equity investment from the Big Society Trust (money transferred from bank accounts that have been dormant for 15 years or more) and the four largest UK banks, each investing £50 million. 'Big Society Capital' aims to develop and grow a sustainable market for social investment in the UK. It was launched in April 2012. The following extract from their website outlines the key aspects of the financing model based on repayable finance.

An emerging social investment market

In the last 20 years, the social sector has moved away from being funded solely by grants and philanthropic donations to a more sophisticated and diverse financing model.

Growing numbers of organisations have looked for ways to make 'repayable' finance work more effectively and efficiently for the social sector. They have aimed to either:

'Recycle' money by investing financial returns generated by social investment in other social sector organisations, creating more impact across the sector, or

Generate a financial return for the investor which makes it possible to raise more capital to go into the sector. There is now an emerging social investment market which is gaining a track record and building expertise. It is developing new ways to connect socially motivated investors with social sector organisations in need of capital.

<http://www.bigsocietycapital.com/the-market/>

3.5.3. Spectrum of financial support and CDFIs

The European Venture Philanthropy Association has developed a model illustrating the spectrum of financial support.³⁵

As the model suggests, funding may be made for purely charitable reasons seeking societal benefits, that is, the 'impact only' segment to the left of the model in the figure below. This is exemplified by the giving by foundations discussed in section 3.5.1. above.

Or funding may be made for financial reasons where the societal benefit is secondary or simply an additional incentive (towards the right of the spectrum).

Other types of philanthropic funding expect a social return on the investment and a financial return. The financial return may be deferred, at no interest or below market rate, and funds may be available for recycling — reuse for other ventures, or investors may seek the return of their capital adjusted for inflation with interest.

³⁵ <http://evpa.eu.com/knowledge-centre/what-is-vp/> accessed 1 December 2011.

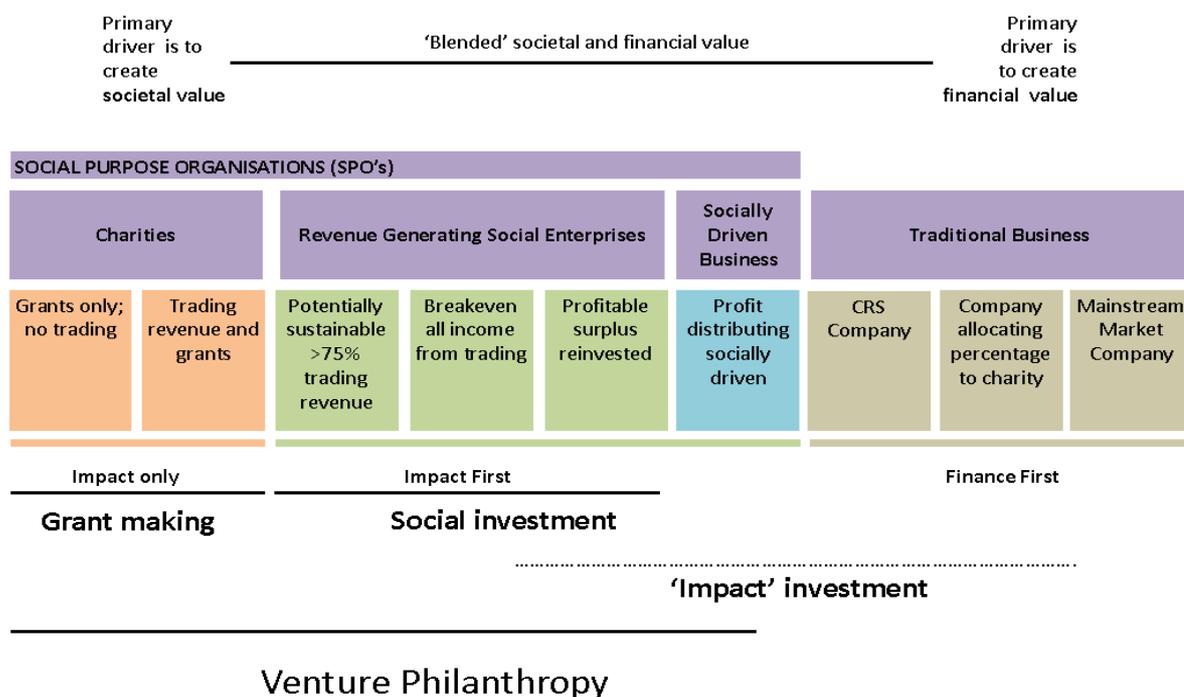


Figure 1: Spectrum of Venture Philanthropy

Adapted from The European Venture Philanthropy Association

Burkett (2010) has suggested that traditional philanthropic sources such as grants are inadequate to sustain social enterprise. However her research also emphasised their importance, particularly in a start-up phase, when enterprises struggle to obtain capital. Some organisations will remain heavily reliant on grants because of the support costs required to achieve their social purpose.

Burkett (2010) identifies four different types of capital required at different stages of a social enterprise life cycle:

- start up/seed capital;
- fixed asset capital;
- working capital; and
- growth and development capital.

In the case of CDFIs, unless they are able to access the resources (premises, desks, computers for example) of an auspicing organisation, they will have all these establishment costs as well as the need to source the lending capital. Furthermore, operational costs may not be fully covered by the income generated from the CDFI loan business.

3.5.4. Demand side barriers

Barriers may also exist in the demand for capital. Lyons et al. (2007) and Burkett (2010) have highlighted the reluctance by boards and management of some organisations to consider sources of income other than grants and traditional philanthropy. A 'grant culture' may be associated with a fear of debt in any form or a lack of knowledge of other forms of equity capital. Developing

appropriate skills and monitoring tools alongside diversification of income sources will be essential if such a grant culture is to be changed (Burkett 2010).

3.6. Summary

In the UK and the US, CDFIs are playing a role in improving the availability of fair and affordable financial services and products to financially excluded individuals who would otherwise not be able to access these from mainstream sources. In Australia, the CDFI sector is underdeveloped compared with other countries.

The concept of financial exclusion is multi-faceted. It includes factors relating to the characteristics of individuals and situational variables (demand-side elements) as well as factors which relate to the characteristics of products, including their availability and affordability.

The available data indicates that financial exclusion is higher amongst those who have low levels of income (and the attendant array of factors which create this, for example, Indigenous or refugee status, educational disadvantage, employment status, age) and low levels of financial literacy. Financial literacy skills are important for some people to assist them to understand and use the available products, even tools as fundamental as ATMs.

Costs of serving these populations have been a disincentive to the development of appropriate financial products by the mainstream financial sector and as noted above, the CDFI sector is undeveloped in Australia. NILS and StepUP are no/low interest options for people on low incomes who need support with basic requirements (household goods, car repairs) based on a welfare model. There are limited options for the 'working poor' and people without good credit history. This gap in the financial services market has led to a growth in high-cost, short-term lending through fringe providers such as payday lenders. There is general agreement that easily accessed, fair, affordable and transparent alternatives are needed if all sections of society are to have the benefits of financial inclusion.

The CDFI pilot program is one strategy currently being supported by the Australian Government to explore the creation of fair and affordable financial services and products to financially excluded individuals.

Within the scope of delivering loans to underserved Australians, the CDFI pilot organisations are taking differing approaches to servicing clients, with distribution channels ranging from Internet based to shopfront and via partner NFPs. The pilot organisations offer smaller personal loans at rates significantly cheaper rates than payday lenders. The CDFIs also have staff available that can assist with budgeting or planning and referral to other supports if required.

As noted by Arashiro (2010 'get ahead' rather than simply 'get by'. Other programs that exist in the Australian context are NILS and StepUP loans programs. These too have been expanding.

The literature suggests that CDFIs may take some time to become sustainable as organisations, and that blended income options combining government, business and private investor support will need to be explored.

4. CDFI Pilot – participating CDFIs³⁶

4.1. Many Rivers

4.1.1. History and background of the organisation

Many Rivers began in Grafton NSW in 2007 as ‘Many Rivers Opportunities’ drawing on microfinance expertise from Opportunity International, a global microfinance organisation operating for over 40 years.

Now called Many Rivers Microfinance Limited, the organisation works to facilitate micro and small business loans in targeted communities in NSW and WA, enabling clients to start and grow businesses. CDFI pilot funding has assisted Many Rivers, to grow from three to nine regional offices. Many Rivers expanded its activities over 2011-2012 and established new offices in Moree and Blacktown, NSW as well as Perth. A new Queensland office opened recently in Cairns and a Condobolin office will open in July 2012 in NSW.

Offices are in:

- Northern NSW — Grafton (office established April 2008)
- Hunter Valley, NSW — Kurri Kurri (office established April 2010)
- Western Sydney, NSW (office established June 2011)
- Moree, NSW (office established June 2011)
- Pilbara, WA (office established September 2010)
- Goldfields, WA (office established May 2011)
- East Kimberley, WA — Kununurra (office established May 2011)
- Perth, WA (office established April 2012)
- Cairns, Qld (office established June 2012)

Many Rivers targets areas of disadvantage, particularly focussed on Indigenous Australians and others at risk of exclusion including refugees and ex-offenders.

Over the course of the pilot Many Rivers Microfinance has reviewed its positioning as an organisation and plans to rebrand as ‘Many Rivers’. This reflects a desire to use simple language (microfinance might be perceived as jargon in the wider community) and reflects its actual role in community development, with a broader remit than the provision of loans. Many Rivers has recently commissioned Access Economics to undertake research into the impacts of its activity.

Organisational structure

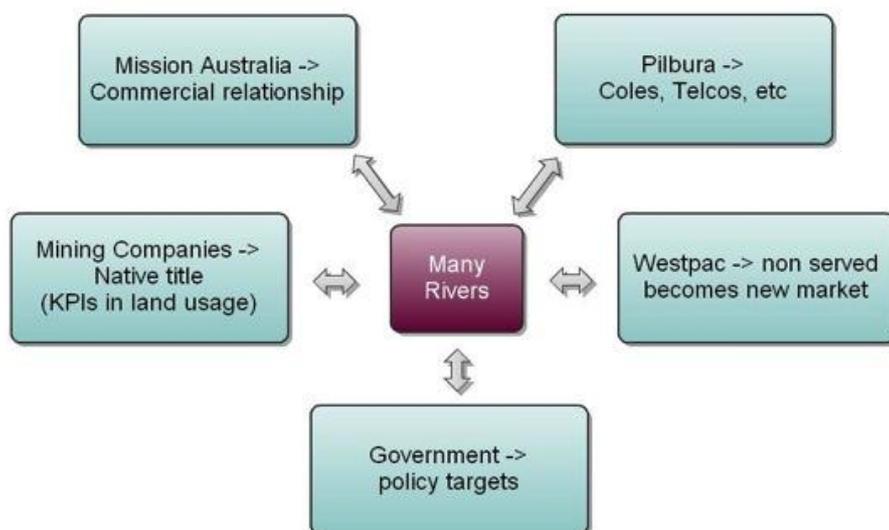
Many Rivers Microfinance Limited is a company limited by guarantee and regulated by the Australian Securities and Investment Commission (ASIC) and the *Corporations Act 2001*. Although a legal entity of Mission Australia for financial reporting purposes, Many Rivers’ strategic and business decisions are taken by its own Board of Directors. Many Rivers Microfinance Limited is a Public

³⁶ It is important to note that direct comparison of the performance between the pilot organisations is not possible, given their very different natures, different time periods of operation and different stages of development. Two organisations were able to lend from the start of the pilot based on their pre-existing organisational arrangements; two first began lending in September 2011, once their CDFIs had been set up and loan capital secured, and one is yet to start lending funds.

Benevolent Institution and endorsed as a deductible gift recipient, so any donations made to it will entitle the donor to a tax deduction. It is also able to fundraise and appeal to the public for funds. Mission Australia's support includes premises and access to the expertise of a large organisation (such as IT, HR), which assists in reducing the infrastructure expenses of Many Rivers.

Many Rivers relies on strong partnerships with supporting organisations that provide funding as well as gifts in kind, such as pro bono legal work for clients.

Figure 1: Many Rivers model



Many Rivers is headed by a leadership team of Chief Executive and Chief Operating Officers. Loans administration is undertaken in the Grafton office.

The service operates through a network of employed Field Officers in each location. The role of the Field Officer includes assessing the viability of the business idea and the commitment of the client to follow through. The Field Officers live and work in the regions they are supporting, and they build the profile of the initiative in their local communities. It is important to Many Rivers that staff are permanent employees rather than casual or contract workers, indicating that Many Rivers is making a long-term commitment to the community.

4.1.2. CDFI pilot activities

Products/ services developed

Field Officers assist people who would otherwise not be able to obtain finance, to develop business plans and apply for loans through Westpac. Unsecured small business loans \$500-\$20,000 are available over periods of six months to three years. The maximum loan for a first time client is \$5,000 for a 12 month term, however after successful repayment further loans are possible as a business develops. Many Rivers has also worked with Westpac to deliver a secured loan product enabling loans of up to \$50,000.

Feedback suggests that a critical role played by Field Officers is encouraging people to share their aspirations relating to work and develop plans to achieve their goals. This may involve a loan but could also involve referral to another program or agency, development of skills (for example in bookkeeping) or encouragement to address barriers to working such as a chaotic home environment or alcohol issues. If they can, people are encouraged to start their business without a loan so that they do not have to service debt as well as start-up costs.

Service delivery model

The role of the Field Officer includes assessing the viability of the business idea and the commitment of the client to follow through. Field Officers may work for several weeks or months with clients to support them in preparing their business plan, assist the client in applying for a business loan if required, and provide follow up as the business becomes established. This may mean occasional contact or regular sessions to assist with ensuring business records are kept. Many Rivers has identified bookkeeping as one of the major challenges faced by its clients.

Loans are provided by and through the Westpac bank, which charges its standard business loan interest rate. Many Rivers markets this as a “real loan from a real bank.” Field Officer support for an application is essential and a loan cannot be applied for if this support is not available. This follows an evidence-based assessment, taking into account the individual's character, capacity and cashflow. Collateral, as loan security, is not required. Before loan documentation is sent to Westpac, there must be endorsement from two Many Rivers' Field Officers (the original Field Officer and one other) and approval by the Chief Operating Officer.

Once a loan is set up the client continues to be supported by the Field Officer who:

- calls the client shortly before the first repayment is due;
- meets with the client to review progress against the business plan and business and personal cashflows at 6 weeks and 12 weeks after the loan disbursement, and then quarterly;
- calls the client at least monthly to provide encouragement and business support; and
- reviews the client's progress against the business plan and business and personal cashflows at the end of the loan.

“In many cases [this] may be first time someone has listened to what they want to do. People expect to be told [what to do].

I help with the business plan and cash flow; people understand bit by bit how the plan works.

This creates a road map for business and their life — maybe for the first time.

We look and see if it is a feasible business, and move into finance options only if needed.

It is important we don't tell [them] what to do — it has to come from within them. They have to own what is happening all the way through and be responsible for their actions.”

Many Rivers Field Officer

Loan repayments are required to be made weekly. Many Rivers deducts loan repayments from clients' bank accounts by automatic direct debit arrangements. The following day, sums are transferred to the loan account with Westpac. If there are any problems in meeting repayments, the Field Officer is alerted by email and will investigate and follow up weekly with the client. One challenge of the role is balancing time between new and existing clients, (estimated as currently about 30 per cent set up 70 per cent existing).

"I am working with 23 people — for about half we talk once a month and that is all they want, the others need a couple of hours every a couple of weeks — some may need face-to-face for half a day if they are struggling with accounts."

Many Rivers Field Officer

Marketing

Local marketing activities are undertaken in each operating region. Examples include: community radio advertising, local business directories, memberships of regional chambers of commerce and other related associations and forums, engagement with local government, participation in community expos and regular and extensive contact with other related service providers in the region (for example Indigenous associations, Community Development Employment Project providers, New Enterprise Incentive Scheme training providers).

Each Field Officer is active in engaging and building networks in the regions in which they work, and Many Rivers reports that the majority of referrals come through word of mouth, employment training providers and local industry and community association networks.

Many Rivers has a website <<http://www.manyriversopportunities.com.au>> and marketing materials including a DVD which contains client case studies.

Many Rivers is considering developing a short workshop as a practical how to start a business. This would act as an awareness raising session, sparking interest and introducing field officers. Bookkeeping skills are the primary requirement of their clients.

4.1.3. Loan policies/ procedures

Many Rivers' policy is not to refuse access to a loan per se, but rather to work with people until they are ready to start their business or they determine it is not an option they wish to pursue. They may be referred elsewhere and Many Rivers works closely with other agencies including employment services.

Arrears policies

Many Rivers takes a long-term view of client relationships and recognises that clients may have occasional difficulties making repayments for business or personal reasons. In these circumstances, Many Rivers may elect to reduce or defer repayments for an agreed period. If a bad debt provision is required the loan is transferred to Many Rivers from Westpac so that the risk is held by the CDFI.

Loans are classified as:

- Green — over 80 per cent of repayments made in the last quarter (reviewed on a rolling quarter basis)
- Yellow — 60-80 per cent of repayments
- Red — less than 60 per cent of repayments — a bad debt provision is created in the financial accounts equivalent to 50 per cent of the loan balance outstanding
- Blue — legal action commenced to recover the loan balance outstanding (with Board approval).

Bad debt provisions are reviewed on a monthly basis based on client repayment performance over the previous quarter and the current loan balance outstanding. There are examples of clients that

have not made repayments for more than one year who then recommence repayment.³⁷ For the four years to April 2012 Many Rivers had not written off any loan balances outstanding.³⁸

Fees & charges

Many Rivers does not charge fees.

4.1.4. Funding

FaHCSIA

FaHCSIA provided \$986,000 (ex-GST) as one-off grant funding to support business development February 2011 – June 2012.

Investors — experience

Many Rivers has a wide range of business partners and sponsors, including resources companies, state and federal governments and foundations. Its strategic partnership with Westpac allows clients to benefit from rates at to the mainstream for loans, even though they would not meet usual lending criteria. Westpac initially became involved through a previous pilot, which was able to demonstrate the viability of the Many Rivers model. Westpac commented in interview that it would have been difficult to present a credible business case for the project as there were too many unknowns/areas of risk. Piloting allowed the project to demonstrate success in loan repayments and arrears management.

“Statistics are about loans — it is difficult to measure a relationship with clients. Many Rivers helps people be comfortable telling their story — telling their dreams and aspirations is a valuable service in itself.

Once they’ve told story they provide things to consider business planning, business set up, marketing, the service isn’t just about the loan — there is lots before.

I am keen to see work around outcomes and outputs — impact measures are very important at community level — it’s a challenge.”

Many Rivers Funder

Under the arrangement with Westpac, the amount Many Rivers can lend is not limited by a capital “pot”. Interest is paid to Westpac (and therefore is not a source of income for the CDFI). In the case of any default, the loan is taken onto Many Rivers’ books.

Westpac is also a main sponsor of Many Rivers activities through grant funding to support operating costs (\$1 million over five years) and gifts in kind including access to Westpac offices in regional areas. The interested earned by Westpac from Many Rivers’ loans is gifted back to the NFP.

Many Rivers also seeks sponsorship of its initiatives from relevant local industries such as the mining industry where there is a business need to provide back into communities, and will aim to grow in areas where there is local support as well as client need.

³⁷ Many Rivers Quarterly Report 01/03/11–30/04/11.

³⁸ Many Rivers CEO AFIN meeting 6 June 2012.

Feedback from sponsors identifies Many Rivers’ key strengths as:

- the relationships built with clients in community
- collaborative working with other agencies — an inclusive approach; and
- integrity and passion about the issues.

“Clients require intensive support — people they are working with can’t operate within mainstream system, there is a lot of work to get start-ups to happen.”

Many Rivers Funder

4.1.5. Pilot progress

Number of loans delivered

As at 13 June 2012, 144 people had been assisted to start or expand existing businesses. Of these, 122 loans have been made and 22 people did not require loans. There was total loan book value of \$668,545. Two clients died during the pilot.

Once a formal loan application is made, the process took an average two working days from application to decision and six working days from decision to receipt of the funds.

The table below summarises the loans made in total by amount. The majority of loans (52 per cent) are for amounts in the range \$4,501-\$5,000.

Table 10: Loans made by amount

Loan Amount (\$)	Total N	%
Loan less than 1,000	1	0.8
1,001 –1,500	3	2.5
1,501–2000	4	3.3
2,001 –2,500	9	7.4
2,501 –3,000	8	6.6
3,001 –4,500	13	10.7
4,501 –5,000	63	51.6
Over 5,001	21	17.2
TOTAL	122	
Non-financial support	22	

Support services accessed

As at 13 June 2012, 229 people have accessed support with business plans and financial skills and are in the ‘pipeline’ for loans. This means they are actively working with Field Officers however it may take many months before any business is established. Data has not been supplied on the characteristics of such individuals. All clients have ongoing support with financial literacy in the context of preparing their business plans and other working tools.

“My process is to start by meeting people who are interested. I ask questions over a cup of coffee — I then wait for them to reengage, I am not pushing them into a business.

If people come back — we talk cashflow if capacity is there (skills differ). We explore what is possible and what can be achieved. It can take several meetings.

It centres on the client, their skill base, waiting until they are ready to go.

I sometimes use a ‘fair dinkum’ test — I give them something to do, it checks drive and motivation it might be go to a supplier, apply for an ABN — try to get them to do something before we go to the credit committee with the loan application.”

Many Rivers Field Officer

Client profiles/ demographics

The table below summarises the profile of the clients of Many Rivers in March 2011 - June 2012. Of the 142 people classified as clients by Many Rivers (122 loans and 20 non-finance support), the majority identify as Aboriginal or Torres Strait Islander (75 per cent) and earn less than \$50,000 a year (73 per cent). Slightly more men than women have set up businesses. The majority (76 per cent) were reliant on government payments for their main source of income when granted the loan. Thirty per cent of clients are in the age band 25-34 years and 27 per cent are 35-44 years. Eighty-six borrowers live in New South Wales, 55 in Western Australia and one in the Australian Capital Territory.

Table 11: Breakdown of Many Rivers’ clients

Client characteristics	Total N	%
Aboriginal/Torres Strait Islander	107	75.3
Income under 50k	104	73.2
Clients who speak a language other than English at home	1	0.7
Person with a disability	1	
Male	85	59
Female	58 ³⁹	40.8
Wages main source of income	22	15.5
Government payments or no income	122	86
Total clients	144	

How many people met their loan obligations?

Of the 122 loans Many Rivers made during the period (March 2011–June 2012), 76 people (62 per cent) were up-to-date with their loan repayments at the end of this period. Thirty-two people were in arrears (26 per cent), and 14 loans had been fully repaid (12 per cent).

Clients that have not made a due payment are followed up by their Field Officer as soon as a repayment is missed. Many Rivers encourages clients to advise if there are business or personal issues impacting on repayments and the organisation will negotiate reductions in payment levels or deferral if warranted and approved by Senior Management. A defined escalation process is in place

³⁹ One not stated.

for clients that do not communicate with Field Officers, ultimately resulting in legal debt recovery action if required, there are no clients currently in this position.

Loan Purpose

Examples of businesses supported include:

- pet supply business
- lawn mowing
- semi-trailer driver
- kerbing and paving
- honey producer
- taxi service
- florist
- employment mentoring
- café
- mobile food/coffee van
- cleaning/laundry
- health and fitness
- homewares shop
- beautician
- concrete contractor
- pub bistro
- artist
- heritage surveyor

Case studies

*Liz and Ruth**

Indigenous sisters in a Goldfields community have started a cleaning, laundry and ironing business. After only six months of operating Liz and Ruth have secured contracts with a number of local government agencies. These contracts were formalised with pro bono legal support from Squire Sanders, a Many Rivers partner. They are now trialling gardening, home maintenance and handyman services and employ local people on a casual basis as they expand their business.

Warren

In mid-2011 the Many Rivers Field Officer in Western Sydney met Warren, a local indigenous man to discuss an opportunity to set up a lawn mowing business. As part of the planning process Warren was encouraged to assess the marketing potential in his local community. Once he had the commitment of 6 potential customers a loan was issued in October 2011. His customer base has now grown to 22 and he has also secured a contract to maintain 2 multi-resident complexes for a large NFP organisation.

Parklea Prison

In Blacktown, a close working relationship with North West Community Care has led to links with people preparing for release from Parklea prison. The Field Officer visits the prison one Friday evening each month for dinner to discuss business opportunities. Prior to release they assist with ABN applications, business name registration, cash flow projections, and post release microfinance loans and ongoing support are available.

**False names have been used to protect anonymity*

4.2. Fair Finance Australia

4.2.1. History and background of the organisation

Fair Finance Australia (FFA) was established by Foresters Community Finance Ltd (Foresters). Foresters has a long history as a mutual organisation. It operates from a Brisbane shopfront in Bowen Hills, QLD and services South-Eastern Queensland. Membership is open to individuals and organisations with an interest in addressing social and financial exclusion. Foresters describe themselves as a “community development finance institution which works to support financial inclusion through microfinance, social enterprise finance, social investment and not-for-profit asset building”.⁴⁰

Fair Finance Australia lists its aim as: “to increase individual financial inclusion by delivering affordable and accessible small consumer loans in an understanding and compassionate manner”.⁴¹ FFA provides loans to people who are unable to access a loan from a mainstream financial institution or bank.

Organisational structure

Foresters is a company limited by shares, formed in 1999 as a result of the merging of the Ancient Order of Foresters in Queensland and the Australian Natives Association of Queensland Friendly Society Ltd. It is an income tax exempt company established for community service purposes with the single shareholder of Foresters Members Limited which is a company limited by guarantee and structured as a mutual organisation owned by its members.

With a history dating back to 1855, Foresters is one of the credit unions, banks and philanthropic societies exploring the application of innovative social and community investment strategies in Australia, and has published a number of research reports and discussion papers on the topic. The organisation has been involved in microfinance for 15 years. Foresters has established related entities to ensure there are appropriate financial vehicles for its work. Social Investment Australia Ltd (wholly-owned subsidiary) is a wholesale capital-raising company; Foresters ANA Community Trust — a Charitable Trust — can receive charitable investment (DGR status/income tax exempt)⁴² from supporters.

FFA staffing comprised a Full time Manager, two Lending Officers, a Support & Referral Officer, shared marketing and distribution positions, and close involvement of Foresters’ CEO in the leadership of the project.

4.2.2. CDFI Pilot Activities

Products/ services developed

FFA offers loans of between \$1,000 and \$4,000 with one-year to two-year terms to people who can demonstrate financial exclusion. Payments are made directly to suppliers for the exact amount required rather to borrowers. There is flexibility with repayments and borrowers can elect to repay weekly, fortnightly or monthly.

⁴⁰ Foresters Information sheet.

⁴¹ <http://www.fairfinance.com.au/>.

⁴² A small number of NFPs (25,292 in 2008) are eligible to apply for Deductible Gift Recipients (DGR) status from the ATO. Donations to DGRs entitle individual donors to claim tax deductions and allows the NPO to apply for funds from grant makers and philanthropic bodies such as Foundations restricted in who can benefit from their funding. Australian pilot CDFIs with DGR status are CCF and Many Rivers.

Service delivery model

Potential borrowers can phone the organisation, or use an online booking tool, to make an inquiry or appointment to see a lending officer or download an application form from the FFA website <<http://www.fairfinance.com.au>>. FFA also receives referrals from a wide network of community organisations. FFA reports that phone inquiries are running at an average daily rate of 6-10 calls.

Interviews are conducted at the main Bowen Hills shopfront, however loan clinics are also run each week from a number of outreach locations, including Kyabra Community Association, the new Caboolture Hub, Nerang Neighbourhood Centre and Palm Beach Neighbourhood Centre (fortnightly). Typically loan application interviews may last 1½ hours. Applicants are briefed about how the loan process works and a loan calculator is used to provide transparency around the cost of the loan. Clients are also taken through a budget process and given some basic financial literacy information. Income statements. Credit checks are undertaken, but only where it looks like a loan is affordable, so as not to impact on the number of credit checks on record. FFA requires that clients take responsibility for any outstanding defaults and will assist in negotiations with creditors to reduce outstanding debts. For clients who are not eligible for a loan, support is provided to individuals to assist them with their financial situation. This might mean providing financial education, or outlining other options that may be available.

In January 2012, FFA became accredited to offer loans under the NILS program for clients for whom this is a more suitable product, as part of a strategy to become a 'one stop shop' instead of having to refer outside so that the client has to go through a second application process.

Marketing

FFA has developed a variety of marketing materials with a common branding and logo, underpinned by a website <<http://www.fairfinance.com.au>>. Marketing materials also include a presence on Facebook, Twitter and YouTube, a brochure and networking events for local agencies working in financial inclusion.

FFA has developed extensive networks with local community organisations. These organisations can be a source of client referrals, but FFA acknowledged that finding the right group of people who could most benefit from their product had been a challenge.

4.2.3. Loan policies/ procedures

FFA are clear that loans will only be approved where a clear benefit to the client can be demonstrated. In this sense, loans are seen as a means to:

- prevent debt spiral;
- increase quality of life; and
- assist the client to develop financial sustainability.

Compliance Issues

After the pilot period Foresters advised the Department of a compliance issue related to its advertising of interest rates on its website. Foresters remedied the incorrect information immediately upon notification by ASIC and accepted the infringement imposed. This issue did not affect their contract documentation which complied with the regulatory requirements. This issue raised the need for continued education and monitoring of newly created CDFIs in terms of compliance with relevant legislation.

Arrears policies

Loan repayments are generally managed through direct debit arrangements. FFA has a direct debit agreement with NAB. There is considerable flexibility in loan repayment and clients can call in if they have difficulty making a repayment. This can either be rescheduled, or skipped and added to the loan term if genuine hardship reasons are provided.

Fees and charges

The current loan is 35 per cent (APR), which is principal and interest. This equates to an effective interest rate of 19.95 per cent on a 12-month term or 20.2 per cent on a 24-month term. FFA does not charge an application fee or on-going loan management fees.

4.2.4. Funding

FaHCSIA

FaHCSIA provided \$2,040,000 to FCF to support the establishment of the CDFI.

Investors

Loan capital to support FFA lending has been provided by NAB. At the outset of the pilot, FFA experienced some delays in finalising the initial capital arrangement from NAB resulting in delays to their lending from a target commencement in May 2012 to September 2012. The loan capital has been made available through the mechanism of an overdraft facility of \$1 million to FFA. An interesting learning for FFA has been that they haven't required a large amount of capital to provide the loans, currently having drawn down only about \$165,000 (supporting 61 loans). This is because of the short-term nature of the loans, which means the capital is recycled quickly. As an overdraft facility, the loan capital is not available for alternative investment on which to generate additional income for the organisation.

The organisation reports that there is joint concern at FFA and NAB about reputational issues around microfinance in the Australian context, which mean that there is pressure to ensure only quality loans are made and hence bad debts are kept to a minimum.

4.2.5. Pilot Progress

Number of loans delivered

As at 13 June 2012, 127 applications were made for loans, of these almost half resulted in loans made (61 applications) and over a third were declined (41 applications). Of the remainder, 23 withdrew or did not take up a loan and two are awaiting decision.

The total loan book value is \$164,402.

Over the past three months, the average waiting time from application to decision was 3.63 days and from decision to receiving loan was 5.91 days. However, FFA are committed to being responsive to client needs and provided examples of loans approved within a one-day turnaround when needed.

FFA is flexible about both the amounts it lends as can be seen in the tables following. While over 40 per cent of loans are in the range \$3,001–\$4,500, 20 per cent of loans are for less than \$1,500.

Loan terms vary from 9 to 24 months. Loan terms tend to be shorter for lower amounts and longer for larger amounts.

Table 12: Loans made by amount

Loan Amount (\$)	Total	%
Loan less than 1,000	3	4.9
1,001 –1,500	10	16.4
1,501 –2,000	6	9.8
2,001 –2,500	7	11.5
2,501 –3,000	7	11.5
3,001 –4,500	26	42.6
4,501 –5,000	2	3.3
Total	61	100.0

Support services accessed

A total of 520 enquiries have been made about the Fair Finance product since the product was launched on 26 September 2011. Of these, 122 people had attended financial literacy/budget support sessions offered by FFA, including those who did not receive a loan.

Client profiles/demographics

The table below summarises the profile of the FFA clients in March 2011–June 2012. About a third of borrowers have a disability and eight per cent identify as Aboriginal or Torres Strait Islander, this is the smallest proportion of all the CDFIs.

Sixty clients live in Queensland and one in NSW.

Table 13: FFA loan clients

Client characteristic	Total	
	N	%
Aboriginal/Torres Strait Island descent	5	8.2
Clients who speak a language other than English at home	4	6.6
Person with a disability	21	34.4
Income under 50k	32	52.5
Male	22	36.1
Female	39	63.9
Primary source of income – wages full/part time/casual	13	21.3
Unemployed/government payments	48	78.7
Total loan clients	61	100

And those refused access?

Forty-one loan applications were declined, all of these were people with a gross income of less than \$50,000 per year. In over 68 per cent of these decisions (28 of 41 applications), the primary reason was negative uncommitted weekly income, so that the applicant would be worse off per week with the loan as they had no ability to make repayments.

FFA emphasises the importance of offering support to all applicants, over thirty referrals were made to Financial Counselling, Centrelink or community programs.

Table 14: Main reasons FFA loan declined

Main reason loan declined	Total	% of declined
Customer already overcommitted financially	3	7.4
Unpaid defaults	2	4.8
Negative Uncommitted Weekly Income (UWI) [i.e. customer would be worse off per week with the loan in real \$ terms]	29	70.7
Client withdrew or did not provide required information	7	17.1
Total declined loans	41	

How many people met their loan obligations?

Fifty-one clients had met all their loan obligations to 13 June 2012. Ten clients had at some time had a dishonoured direct debit repayment. All clients were contacted and agreed to make the repayment up or have negotiated a payment variation to their loan. No loans were still in arrears at the end of the reporting period.

Loan Purpose

The table below lists the primary reason for borrowing from FFA.

Table 15: FFA Purpose of loans

Purpose of loans	Number of clients primary reason	%
Pay bills	7	11.5
Buy household item	2	3.3
Car rego/repairs	6	9.8
Pay off other credit	15	24.6
Education expenses	3	4.9
Medical costs	1	1.6
Start business	2	3.3
Moving house/bond	7	11.5
Other	18	29.5
Total	61	100.0

Case studies

Joyce

An ex-business woman, now a pensioner, Joyce went through a very traumatic experience of being a victim of a scam for 4 years which cost her time and money. Her husband then left her and also her children who were frustrated when she initially did not want to believe she was being scammed.

By the time Joyce realised she had nothing left, her health was affected. She was depressed and had attempted suicide a few times. During the period she was ill, she also missed some of her rent payments and the landlord (private rental) had only picked it up after trying to reconcile her account for her tax returns. By then the amount had increased to almost \$4,000.

Fair Finance Australia was able to assist client get back on track and help her secure a cheaper rental property with her now clean rental history. She is a great advocate to help others get their lives back on track after being scammed as there are a lot of people who are too ashamed to contemplate seeking help after they had been scammed. She never thought she would have got herself into such a situation but it happened and she hopes she could help others after her experience.

Scarlett

Scarlett needed a loan of \$3,114 to pay remaining course fee to obtain Certificate IV in Fitness.

Scarlet, who is a single mum with two children aged two and six years, completed a Certificate III and IV in Fitness with the Human Performance Centre. The course fee totalled \$4950, which she was on payment plan for. Unfortunately, the client could not receive her two Certificates until the total course fee was paid. This meant she was also unable to begin practising as a personal trainer/fitness instructor.

She also had a default on her credit history which she was unaware of, rendering her unable to get a loan from any other financial institution to pay out her course fees. The loan from Fair Finance enabled her to pay her course fees, rectify her credit history, and begin her own business as a personal trainer and fitness instructor.

4.3. In-roads

4.3.1. History and Background of the organisation

In-roads is an initiative of Community Sector Banking (CSB). CSB was established in 2002 as a joint venture between Bendigo and Adelaide Bank and a consortium of twenty NFP organisations. Its vision is “to be the financial institution that strengthens not-for-profits in delivering social change”.⁴³

Organisational structure

In-roads is a partnership between CSB and seven community organisations (see list below) across Australia. Bendigo Bank via Community Sector Banking provides the loan capital and back office administration, while the community organisations’ expertise is used to provide outreach to clients and support them with their loan application and any associated budgeting or financial literacy support that may be needed. In-roads is a brand used to unite the seven partnerships rather than existing as a legal entity in its own right.

Partners received funding from CSB to cover costs such as recruiting suitable staff (known as Relationship Managers), marketing and equipment. They were also provided with training in loan procedures. Partners made loan recommendations, but the actual decision to lend was made by a Community Sector Banking loan officer based on criteria agreed with Bendigo Bank. Relationship managers have been recruited and trained to promote and manage In-roads in their area and they link by web-conference with CSB.

The partner organisations are:

- Access Community Group [ACG] New South Wales;
- Anglicare South Australia;
- St Luke’s Anglicare Victoria;
- Centre for Aboriginal Independence and Enterprise (CAIE) South East Queensland;
- Traditional Credit Union (TCU) Northern Territory;
- Kimberley Employment Service (KES) West Australia; and
- O Group Tasmania.

The model draws on CSB’s experience with a loans pilot with the Brotherhood of St Laurence in 2003-2005.

Central CSB staffing of the pilot comprised a Project Manager, who was involved in the of the new initiative (this role has now concluded), Executive Director oversight, two lending officers and administrative support.

Each partner organisation has implemented In-roads in a different manner; their working arrangements and feedback on the pilot are reported in section 4.4.8 following.

4.3.2. CDFI pilot activities

Products/ services developed

Loans of between \$500 and \$3,000 are offered to people who meet the following criteria:

- Australian citizen or permanent resident over 18 years old;

⁴³ <http://www.communitysectorbanking.com.au/our_story/our-beliefs> accessed 26 May 2012.

- annual household income less than \$50,000 (gross) inclusive of benefits and pension payments;
- hold a Health Care Card or Pension Concession Card or receive Family Tax Benefit Part A;⁴⁴ and
- demonstrated ability to make regular payments (for example, household budget, credit record, bill payment history).

If an applicant is successful, the agreed loan is paid directly to the goods/ service provider who is meeting the loan purpose. Repayments are made by direct debit.

Some of the partner organisations also offer access to NILS and StepUP loans, each of which are cheaper than the In-roads loan. As these are cheaper for borrowers, they can be the preferred product for some, however not all people seeking loans will be eligible for NILS and Step Up.

In some cases the NILS process can be slower and In-roads has been preferred because a fast decision is essential (for example, paying for a funeral). Partners also reported that some communities prefer to deal with people they know and feel they can talk to, and this will be more important than the cost of the loan.

“The issue here is not the availability of credit but the appropriateness of it. It’s not ethical to lend if you don’t need to.”

Relationship Manager

Service delivery model

The CSB In-roads model takes the form of ‘hub and spoke’, with a central banking function making decisions on lending and all aspects of account creation and management and community sector partner organisations working at the ‘front line’ with clients.

The service delivery model depends on the In-roads partner. In some instances a dedicated member of staff has worked solely on promoting the product and meeting with clients, in others the work has been shared among staff with a wider remit such as financial counselling services.

Three partners have a focus on working with Indigenous clients (although support and loans are available, and have been made, to non-Indigenous people).

Marketing

Each outlet/ partner shares common ‘In-roads’ branding and a website <<http://www.in-roads.com.au/>>. Promotional activities reported by partners include:

- development of relationships with other organisations to establish a referral base and build awareness;
- media work (free and paid advertising, TV and radio coverage); and
- visiting remote communities.

Each partnership organised a local launch and associated publicity including press and radio. Materials developed include a standard In-roads leaflet, tailored with a panel specific to each partner for each state and territory. A DVD with client interviews and case studies, and website <<http://www.in-roads.com.au/>>.

⁴⁴ Applicants without pension cards are referred directly to CSB for loan interviews.

There is a single phone number '1300 INROAD' — 1300 467 623 that directs callers to the partner organisation in each state and territory.

4.3.3. Loan policies/procedures

All partners have to operate in a consistent manner and in accordance with the In-roads policies and procedures, which were developed with Bendigo Bank.

The partners' role is to refer clients and assist them in calculating if a loan is affordable.

There is a full operations manual and standard documentation for all aspects of the lending process from initial enquiry to application. Detailed checklists ensure that Relationship Managers can support clients in their application and check that all required documents are forwarded to CSB.

Arrears policies

CSB identifies any accounts in arrears. In this situation, an email is sent to the Relationship Manager who follows up with the client and works with them to develop repayment plans. Feedback from partners is that this is very effective. CSB has initiated a system with Bendigo Bank that provides access to daily reports on arrears for all In-roads clients.

Procedures are in place for escalation of the process at 9 and 19 days in arrears if necessary, and after 50 days recovery action is instigated if there has been no contact from the client. However clients are always encouraged to discuss any issues or hardship with their Relationship Manager and arrangements can be made to assist with financial difficulty. Relationship Managers reported that this was working well and they were usually able to find a solution. In some cases family members assisted if a person was not able to make a repayment for example.

Fees & charges

A \$50 fee is charged for the application. This is refunded once an outstanding balance is repaid in full. Loans are offered at 13.95 per cent APR fixed for the period of the loan.

4.3.4. Funding

FaHCSIA

FaHCSIA provided \$2,170,000 (ex-GST) as one-off grant funding to CSB to support business development February 2011 - June 2012.

Investors — experience

CSB is a franchise of Bendigo Bank and needed to have the support of Bendigo Bank in order to establish the CDFI. CSB operates under Bendigo Bank's credit licence and is subject to audit by the bank. Bendigo Bank has allocated \$1 million for In-roads lending from its balance sheet. CSB reserves \$200,000 to take first loss risk (protecting Bendigo Bank from risk through borrower defaults).

In terms of future capital growth, CSB intends to establish a Social Investment Account for individuals and a Social Investment Fund for NFPs. This will provide opportunities to secure deposit funds, and assist in building the capital pool for In-roads, while allowing investors to achieve a commercial return on their deposit. The interest earned through investment of the capital pool would create an income stream to support In-roads.

CSB is also investigating facilitating cloud funding, which uses social media to attract multiple small donations, in support of social entrepreneurs.

4.3.5. Pilot progress

Given the complex nature of the partnership arrangements, and the need to agree to appropriate loans documentation and procedures for the initiative with Bendigo Bank, In-roads took considerable time to become established. Although some of the partnerships launched early in August, initial lending was not possible until late September 2011. This loss of momentum was reported by some partners to be a problem in creating awareness of the product.

Number of loans delivered

As at 13 June 2012, 158 loans were financed since lending began in September 2011 with a total value of \$423,181. Loans are made with a 24-month term.

1,201 enquiries about In-roads were recorded; 274 loan applications were made to CSB of which 158 were approved. One hundred and forty-seven referrals are recorded. The most common referrals were for financial counselling (about a third of cases), to a creditor or for NILS.

The average waiting time from application to decision was 6 days and the average waiting time from decision to receiving the loan funds was 17 days. In some cases the delays in funding may be attributed to the need for supplier invoices for payment by CSB.

Almost 87 per cent of loans are for amounts between \$2,000 and \$3,000. Loan terms are 24 months.

Table 16: Loans made by In-roads

Loan Amount	Total	%
Loan less than 1,000	2	1.3
1,001–1,500	7	4.4
1,501–2,000	12	7.6
2,001–2,500	22	13.9
2,501–3,000	115	72.8
Total	158	100

Support services accessed

Relationship Managers offered a range of services to clients including support with financial literacy, as well as counselling, housing or employment services.

Client profiles/ demographics

In-roads' performance report provides the following data on loan clients. All have gross annual incomes of less than \$50,000 and 63.9 per cent identify as Aboriginal or Torres Strait Islanders. Over a third have a disability. A significant proportion of borrowers (82 per cent) are on Centrelink payments.

Table 17: In-roads borrowers

Client characteristic	Total	%
Aboriginal/Torres Strait Islander	101	63.9
Income under 50k	158	100.0
Clients who speak a language other than English at home	1	0.6
Person with a disability	57	36.1
Male	52	32.9
Female	106	67.1
Primary source of income – wages full/part time/casual	34	21.5
Government payments	124	78.5
Total loans	158	100

The In-roads pilot has made most loans in WA in the Kimberly region (59 loans). The next highest number is in Queensland (44 loans). Both these partner organisations have an Indigenous focus and this is reflected in the high number of loans made to people identifying as Aboriginal or Torres Strait Islander. These two organisations contributed 65 per cent of the total loans. Four loans were made in the Northern Territory and eight in South Australia, the least active areas for In-roads.

Table 18: State of residence of In-roads borrowers — indicating levels of activity by partners

State	Number of borrowers	%
NSW	20	12.7
NT	4	2.5
QLD	44	27.8
SA	8	5.1
TAS	10	6.3
VIC	13	8.2
WA	59	37.3
Total	158	100

And those refused access?

Of the 274 applications received during the pilot period, there were 80 declined (29 per cent). The main reasons for decline were the applicant's existing level of debt or a significant history of defaults.

One difficulty experienced by In-roads related to the disclosure of personal financial information about clients to the Relationship Managers. For example, if an unpaid default was discovered by In-roads during the credit check process, privacy protocols meant that until May 2012 CSB were

unable to share that information with Relationship Managers who were dealing with the applicant. Sometimes, applicants may be unaware that there is a default on their credit history. In-roads worked with Bendigo Bank to seek legal advice and develop a solution on this matter and from late May 2012 have been able to share information on client credit history (with their permission).

Table 19: Main reasons In-roads loan declined

Main reason loan declined	Total	% of declined
Customer already overcommitted financially	17	21.3
Unpaid defaults	55	68.8
Client withdrew	5	6.3
Other	3	3.8
Total declined loans	80	100

How many people met their loan obligations?

Of the 158 borrowers, fifteen (5 per cent) had not met their loan obligations in the reporting period to 13 June 2012. In-roads advised that in all but three cases the arrears relate to one or two missed payments and are not significant. In three cases (less than 2 per cent) arrears are problematic and loans may have to be written off.

“It was a surprise. I thought the role would be about writing loans. I was floored at how readily accessible money is and how badly people can manage. People’s understanding about their obligations to their creditors is staggeringly low. We are the ambulance at the bottom of the cliff.”

Relationship Manager

Loan purpose

The In-roads data details the primary reason applicants applied for loans. The majority relate to vehicle issues or buying household items. In the interviews and survey undertaken by WestWood Spice it is clear that borrowers may actually arrange a loan with two purposes (for example, to clear a bill with a default and also to pay for a car repair) however data has not been collected to detail this.

Table 20: Purpose of loans

Purpose of loans	Number of clients primary reason	%
Pay bills	2	1.3
Buy household item	60	38.0
Car rego/repairs	37	23.4
Pay off other credit	12	7.6
Celebration	1	0.6
House repairs	2	1.3
Medical costs	4	2.5
Start business	1	0.6
Moving house/bond	5	3.2
Other	34	21.5
Total	158	100.0

4.3.6. Partners

Centre for Aboriginal Independence and Enterprise (CAIE)

The CAIE was formed to foster cultural, social and community expression and assists to realise enhanced self-esteem and economic independence for Aboriginal people. In 2008, CAIE was funded to undertake research into the creation of an Indigenous controlled financial institution in South-East Queensland. Working with CSB on In-roads provides an opportunity to further explore the needs of Indigenous people and financial products, especially credit.

“Blackfellas have no history with banks. The old folk had horrific experiences with stolen wages and being refused service, and they pass that down. We make people feel okay, we approach things informally.”

CAIE Team

Implementing the pilot

CAIE specialised in loans to the Aboriginal community around Ipswich, with outreach into rural communities. CAIE had two staff who actively worked on In-roads. When visiting an area, CAIE would start by talking with elders and people in authority to explain In-roads. If elders were happy then CAIE would be invited back to meet individuals.

Pilot performance to 13 June 2012

Through CAIE, CSB has made forty-four loans totalling \$109,646. CAIE reports strong interest in the program and received 136 enquiries about In-roads during the pilot period. Twenty people took part in financial conversations and training, including one group session for eight people, however CAIE emphasise the importance of privacy for people in discussing needs and wants and have not found that people want to commit to multiple workshops.

“Clients are dejected if they are knocked back, but we can help them try again if they want to. In one case we encouraged a young person to prove he would be able to repay a loan by saving the amount he needed each week. After 6 weeks he was able to bring in the bank statements showing he had managed to save and have a loan approved.”

CAIE Team

Learning points

CAIE’s experience with working in Indigenous communities presented a number of learnings including the:

- importance of working in a culturally competent manner in different communities;
- challenges faced with working in remote areas, including cost and communications; and
- difficulties with the loan application—many clients reported feeling intimidated by this.

CAIE and their clients saw In-Roads as an important path to mainstream finance. CAIE staff described the program as providing “a loan not a handout”, thereby encouraging self-determination and building confidence. The staff believed about 80 per cent of their clients have used Cash Converters or similar organisations for loans. After an In-Roads loan clients say they are “not going back to Cashies”.

The CAIE team believe that key to their success has been their high profile within the community, the trust that has been built and their personal holistic relationships with clients. They noted that momentum was important in building the In-roads name, with the delay in starting the program damaging this.

O Group

O Group is an employment service, with fourteen offices across Tasmania. Services include disability and rehabilitation work, apprenticeships and other forms of mentoring and training. Its vision is to be recognised for the provision of quality, responsive and sustainable community infrastructure and support services through direct intervention and partnerships.

In the view of O Group, working with In-roads has been a good fit because the role of credit in the pathway to employment. In-roads has also been developing small business loans and that would work well for O Group.

"In Tasmania you can walk in any direction for 5 minutes and can touch five payday lenders."

Relationship Manager

Implementing the pilot

The Relationship Manager was appointed in July, although lending did not start until September. Key aspects of the relationship manager's role included:

- understanding the client's financial situation;
- providing referrals to financial counsellors or assisting client to ring creditors directly;
- assisting clients with paperwork; and
- promoting and raising awareness of In-roads within O Group and other agencies.

Should the pilot be extended, O Group is exploring a different model of service delivery, whereby all small business advisers will have responsibility for the In-roads program and the role of the relationship manager will end.

Pilot performance to 13 June 2012

Through O Group, CSB has made 10 loans totalling \$26,406. O Group reports they have had about 190 genuine enquiries, translating to about 5 per cent with loans. Typical customers were single mothers, often leaving a relationship with outstanding debts. These formed about half the client group. A number of referrals were made to O Group from Bendigo Bank, particularly if clients did not want a credit card then In-roads was recommended for smaller amounts.

Learning points

O Group noted that while delays with pilots are inevitable, there was a loss of momentum not being able to start lending until September. The close working relationship between CSB and O Group helped with the reducing the frustrations of O Group staff about the delays.

The O Group team noted the substantial amount of time needed to work one on one with people to improve financial literacy. This was helped when positive working relationships were built with other agencies in support of clients, such as having a financial counsellor sit in on a session with a client.

Kimberly Employment Services (KES)

KES is an Aboriginal organisation with a strong network in rural and remote areas. KES was formed in 2003 to harness local skills and knowledge in delivering employment services in the Western Kimberly. It is based in Broome, with offices in Fitzroy Crossing and Derby.

Implementing the pilot

KES appointed a relationship manager dedicated to the In Roads pilot. Initial work required regular visits to remote communities and meetings with key people in the community, especially in areas where there are initiatives building houses. The Relationship Manager noted that word of mouth was essential in promoting the program, particularly the role of women elders. The key to building relationships in remote communities was trust.

“It is the first time my clients have ever taken out a loan. They don’t deal with banks, in the past they have been told to go away because they don’t earn enough.”

KES Relationship Manager

Pilot performance to 13 June 2012

Through KES, CSB has made 59 loans totalling \$169,891. Forty of the 43 loans made in the last reporting period were to people identifying as Aboriginal or Torres Strait Islander (93%). 19 people have a disability (44%). All clients earn less than \$50,000 gross income a year. The most common reason for borrowing is to purchase household items (88%). Loans are all \$2,000-\$3,000 for 24 months.

“The true value of the program is when, for many people for the first time, they have to work out what their income is and where their money goes.”

KES Relationship Manager

Learning points

Meeting demand was recognised by KES as a substantial issue for the pilot. The Relationship Manager described incidences where people had to wait for two hours or more to talk with him. This was exacerbated by the long distances involved and the poor quality of communication technologies. The Relationship Manager also reported that he had been ‘inundated’ with calls associated with new building initiatives in remote communities—“people had houses but nothing to sit on or wash their clothes with”. This also created problems with the post loan process, which was described as time consuming given the difficulties of finding suppliers for goods and getting these delivered. KES reported that it was not unusual for 10 per cent of a loan to be required for logistics.

KES reported already seeing benefits from the In-roads program. They have received feedback that people feel more confident with the loan and that it has improved self esteem.

KES compared the In-roads product to a NILS loan. While their clients knew about NILS, In-roads was seen as faster, less cumbersome and communities see results quickly. There are visible and tangible results. This was seen as important in an area where there are lots of abandoned projects.

“When we examined Rita’s bank statement I noted a payment to a payday lender. After calculating her payments, we discovered she was paying back almost double the principal. We worked with the client to discharge the debt then her to get an In-roads loan. She vowed she would never go to the payday lender again.”

KES Relationship Manager

Access Community Group (ACG) Client profiles/ demographics

Access Community Group (ACG) is a NFP with a focus on community development and social justice, working across the Illawarra, South Coast and Southern Highlands of NSW. Ninety per cent of ACG clients are on low incomes. Services are in the areas of employment, training, post release support, youth work and recruitment solutions.

“Ones that have fallen behind get the benefit of the doubt. We call and ask can we help?”

ACG Relationship Manager

Implementing the pilot

ACG appointed a Relationship Manager to In-roads, supported by a program manager. Marketing for In-roads was done through other NFP service providers and wide interest was shown in the program, even as far as the Central Coast. Clients were interviewed for the loan, during which most of the financial education took place. Interviews took anywhere from 30 minutes to three hours. ACG initially tried offering financial education courses, however there was a general lack of interest in these. Most client interviews were in the Corrimal offices, but there were also outreach sessions in other offices and community centres.

Pilot performance to 13 June 2012

Through ACG, CSB made 20 loans totalling \$48,688.

Learning points

ACG reported many positive impacts for their clients from the pilot. These included relief from financial stress, increased self-confidence and increased feelings of empowerment—“people were embarrassed to have financial problems, however with In-roads they can start to see how to resolve these.” ACG noted that while their launch in July was very successful, delays with being able to lend lost a substantial amount of momentum.

Like KES, ACG also saw differences between NILS and In-roads. The Relationship Manager noted that while there was some initial pushback from NILS coordinators, they refer between NILS and In-roads. “It is clear that the product meets different needs.”

Finally, Centrepay was identified as having an important role to play in financial management. The Relationship Manager commented that “people are used to having bills taken out, they have to learn not to withdraw everything which can be hard.”

Case Study

Pat

Pat was referred to ACG by Wollongong women’s services, a refuge for women. She had been through a very tough time and was now trying to make something of her life. She had been moving from place to place to escape her past and now she wanted to move forward. During her moving around she incurred a lot of debt and it became out of control. As she was moving she never changed her address with her creditors and this just built up. She also went to payday lenders for a quick fix to get her out of trouble but ended up in an even worse situation.

She then made an appointment with ACG and did the application but due to the massive debt Pat would not be eligible. The Relationship Manager was able to go through her financial situation and assist her with getting her debts in line.

Although her financial situation was poor, we were able to explain to CSB why a loan was in the client’s interest — we got approval. Since then the client has been in constant contact with us regarding her budget and is trying to stay in line with it. She has advised that since her payday loans have been sorted she has been able to save and move back in the right direction.

St Luke's Anglicare

St Luke's Anglicare assists people to make positive changes in their lives, to be connected and contribute to their communities. They are an NFP working across North-Central Victoria and Southern New South Wales, employing more than 360 people in areas including disability, mental health, family support and youth services as well as financial counselling. St Luke's also offers a NILS program.

"If there are any issues for the client it is not a '1800 who cares' number. If they have an issue they ring up and talk to St Luke's, so they have confidence. We are the front line."

St Luke's Team

Implementing the pilot

In-roads sits within the financial counselling team coordinated by a team leader.

Loans made to 13 June 2012

Through St Luke's, CSB has made thirteen loans totalling \$36,391. Sixteen enquiries were received 21 March-13 June 2012 and seven successful loan applications were made, none declined. All applications were from people earning less than \$40,000. The main purposes are vehicle related.

Learning points

Like other CSB's other partners, St Luke's noted that the slow start was a big issue for their organisation and they commented that the pilot needs a longer implementation time to gain traction.

St Luke's discovered that In-roads was a good fit as part of a suite of products and that it was "not a one-size-fits-all approach." St Luke's saw In-roads as a good product for people moving out of its core group of clients (who may be in crisis or reliant on welfare and emergency payments) and back to mainstream financial services. They noted that at times people came to talk about In-roads but were referred for NILS and vice versa. St Luke's believes that In-roads could work well with Good Money Hubs as a one stop shop with street frontages and would like to see it work across Victoria.

There were some issues identified by St Luke's, particularly the need to avoid any potential conflict of interest for financial counsellors. St Luke's achieved this by making sure different people provided information about the loan product. St Luke's noted this was less of an issue than originally anticipated. Like ACG, St Luke's highlighted the need to use Centrepay for In-roads repayments.

Anglicare SA

Anglicare SA Inc is a large NFP which operates independently with its own management structure and its own Board of Directors, while retaining strong links with the Anglican Church. In-roads sits in the Financial Wellbeing team of the Community Engagement and Strengthening portfolio. The team of 33 staff provide a number of emergency assistance programs in South Australia, including support for gambling and the operation of a Food Barn. Other programs operated to assist with financial inclusion are NILS®, Financial Counselling, Budget Counselling, Saver Plus and low income support.

"People really like that they can pay back a loan and learn how to manage their money."

Program Manager

Implementing the pilot

Anglicare engaged a qualified financial counsellor to assist with the implementation of In-roads. Phone inquiries were triaged through particular services offered by Anglicare and those for whom In-roads was appropriate were sent an information pack. A face-to-face appointment was organised within 3 days and a financial counsellor assisted with people's budgets. Loan paperwork was also completed face-to-face. People who received loans were offered opportunities to participate in financial literacy workshops.

Loans made to 13 June 2012

Through Anglicare SA, CSB has made eight loans totalling \$6,987. Eight-eight enquiries were recorded, in the pilot period (October 2011 to June 2012) Anglicare SA advised from the eighty-eight people they have made sixteen referrals to Financial Counselling, eleven referrals for StepUP loans and two NILS referrals.

Learning points

As with other In-roads partners, the loss of impetus with the delay after the launch caused significant damage to the program's reputation. At the time of the launch there were fifty potential clients who were then unable to be assisted with a loan. Anglicare notes, it would have been preferable to have had the product ready to deliver prior to the public launch.

For Anglicare, the In-roads product was seen as having great potential to be built in as a graded step for progression into mainstream finance, bridging NILS and low interest borrowing and preventing use of payday lenders. Their main target group was described as the 'working poor', and Anglicare felt that some CSB's eligibility criteria were unnecessarily restrictive (such as those on an income above \$50,000 and those who did not have a health care card).

There were two particularly needy groups of people:

- low income earners who were facing reduced income through decreased working hours and are ineligible for entitlements including health care card or Newstart Allowance etc; and
- people who were not NILS eligible, but needed support up to \$3,000.

Other issues identified by Anglicare included the difficulty of the loan application paperwork, particularly for people with poor literacy skills and the lack of a financial literacy framework. Anglicare noted the need to collect social impact data to track client outcomes.

Case studies

Jane

Jane is 66 years old. 4 months ago she finally got the courage to ask her husband of 40 years to leave the family home. Jayne's husband was an alcoholic and had been for many years. Whilst he was never physically abusive to her he would spend every cent he could on booze. Jayne learnt very early on how to hide money and live frugally. However over the past couple of years her husband's drinking got worse and so she resorted to taking out a credit card to cover the mortgage and bills when there was no money, Jayne also took out Radio Rentals to buy essential items such as a new fridge and TV.

Jayne sought the assistance of a Financial Counsellor shortly after her husband left and it became very apparent that she had a lot of debt and unpaid bills. Through the process of assisting her to get on top of things it was suggested she call in regards to applying for an In-roads loan to pay out the Radio Rentals debt that was costing her \$100 per fortnight in payments.

Her loan was approved and now her payments are only \$49 per fortnight leaving her with \$50 that she can use to reduce her credit card debt. Jayne was so happy when she heard the news that she cried and gave her Financial Counsellor the biggest hug she'd had in ages! One month on and Jayne is managing her debts well, she can see the light at the end of the tunnel, and while she will be paying them off for quite some time yet she knows that she can do it. She said that the In-roads loan has meant a weight has been lifted and she can now move forward with her new life.

Peter

Peter was living with his foster parents who had looked after him since he was 13 years old, Peter is now 19. Peter has a mild disability and struggles to read and write, but, on the advice of his hardworking foster parents, had started a lawn mowing round to earn some money; his foster dad assisted him with the purchase of his Ute and he was paying the lawn mower off. Peter had been driving back from a job when his clutch failed. He needed to get the Ute repaired and so Peter and his Foster dad contacted me. We arranged to meet at a Café in a nearby town, and completed the application over a coffee. Peter's loan was approved and he managed to get his Ute back on the road.

That was in November 2011, I recently contacted Peter to see how he was going, he told me he had expanded his lawn mowing round and was now quite busy. If Peter's loan hadn't been approved Peter would be relying on Centrelink solely for his income, whereas now he earning his own income, his foster parents are very proud of Peter and his achievements.

Ben

Ben came to see In-roads in the hope of getting a loan to purchase a Scooter. Ben's life hasn't been an easy one with drugs and alcohol causing havoc over the years, but he finally got it together and 6 months ago he moved into his housing trust unit, finally a place he could call his own.

Ben's goal to get a Scooter was so he could enrol into University and study. He is also hoping to get a part-time job to subsidise his income. Ben was sure that he would be knocked back because of his low income (Centrelink), so he was over the moon when his loan was approved.

Ben is now the proud owner of a brand new Scooter and looking forward to re-joining the academic world. He feels as if he has been given a fresh start and intends to make the most of it!

Traditional Credit Union

The Traditional Credit Union (TCU) was originally established in 1994 by a group of Aboriginal Elders to provide financial services to residents of Arnhemland communities who were disadvantaged by a lack of banking and other financial services. TCU offers a full range of financial products to members, as well as specialised products such as family/clan accounts. Financial literacy education is also offered. TCU initially saw a good fit between the In-roads product and its own approach to lending.

“There is definitely a need, people are paying a \$200 establishment fee and 96 per cent interest for a \$600 payday loan.”

CEO

The credit union has its own loan product available to members. Personal loans are made up to \$5,000 for a first loan (\$10,000 following successful repayment of a first loan) for terms up to 5 years. Loans are only available to members who deposit their pay into a TCU account and who have saved 10 per cent of their loan amount. People have to have saved regularly for 3 months prior to the loan being granted. This means that to borrow \$1,000, \$100 has to be saved in 3 months (\$17 per fortnight). Personal loans can only be used to purchase goods and payment is made to the third party; cash loans are not made. The most common loan purposes are white goods, furniture and car-related expenses. Families will sometimes pool loans to make large purchases. The credit union has a loan book of about \$350,000 and only two clients in arrears.⁴⁵

TCU has a head office in Darwin and eleven branch offices in very remote communities.

Implementing the pilot

TCU was the last of the seven organisations to join the In-roads pilot. There was a public launch of the program linked to the opening of a new TCU branch in Casuarina. As In-roads loans had already been made in other states, TCU did not experience the delays reported by other partners. Marketing following the launch was mainly by word of mouth.

Loans made to 13 June 2012

Through TCU, CSB has made four loans during the pilot period, totalling \$12,000.

Learning points

TCU viewed In-roads as a great product, but noted that it would prefer to make loans from its balance sheet rather than for CSB.

The In-roads model emphasised one-to-one, face to-face lending, and TCU found this impractical and too expensive in the Northern Territory context. Given the distances between branches and customers in the Northern Territory, much of the work the credit union does is by telephone. It still emphasises relationship-building as key to its approach, and believes the ability to speak in a customer’s language is an important factor in its success.

TCU uses simpler forms and accommodates customers who find it difficult to manage paperwork, the credit union found it difficult to get loans “over the line” with CSB because of the different requirements of the two financial institutions.

⁴⁵ CEO interview 4 June 2012.

4.4. Fair Loans Foundation

4.4.1. History and background of the organisation

Fair Loans is an internet-based lending institution.⁴⁶ The organisation restructured in 2010 into a Foundation⁴⁷ and social enterprise, having previously operated as a for profit organisation called Mobile Finance Pty Ltd (trading as Money Fast) offering personal loans and mortgage brokering.

Fair Loans' intent is to be positioned to offer a fair alternative to payday lending to people with poor credit history, defaults or other factors that would make them vulnerable to fringe lenders.⁴⁸ The small loans pilot (NAB 2010) identified that Money Fast's⁴⁹ web-based loan product was attractive to people on moderate incomes (an average of \$859 per fortnight), some with jobs, as well as those with more limited options. As the report Beyond Reasonable Debt (2009) and the NAB study noted, financial decision making is not always based on 'rational' factors, and the convenience, speed and relative anonymity of web-based borrowing may be important in assisting people who otherwise would be financially excluded, whatever the reason for the exclusion.

Fair Loans has also set up CDFI.AB as a wholly owned division of the Foundation, offering loans to the Indigenous Community using a specialist mobile money manager (the Indigenous engagement worker). CDFI.AB has its own Board.

The Fair Loans Foundation and CDFI.AB has supported two projects at Werrington Public School. The first aims to strengthen the engagement and connection of Aboriginal students, their community and the school community. The second project provides \$10,000 over three years to support the work of an Aboriginal Education Coordinator at the school.

"By taking an entrepreneurial approach and embracing technology, we can harness the power of the internet to provide the lowest rates possible to the broadest population, in the shortest possible time."

Fair Loans presentation

Organisational structure

As a web-based lender, Fair Loans' business model relies on achieving scale both in terms of numbers of loans and capital pool. The NAB pilot (2010) indicated that loans for less than an average size of \$700 over periods shorter than a year could not be offered sustainably in compliance with regulations in states with a 48 per cent per annum cap (NAB 2010).

Fair Loans has a senior team of two people, three loans officers managing day-to-day client applications and funding, a specialist Indigenous engagement worker based in Mount Druitt and Money Mentor (until early June 2012).

⁴⁶ Fair Loans website can be accessed at <<http://www.fairloans.org.au>>.

⁴⁷ As a charitable foundation, Fair Loans is an organisation whose purpose is to give money away for community benefit. The legal term "Trust" also refers to this type of organisation. Foundations have a board of trustees and are restricted by the regulations governing their legal structure (Meachen 2009). As a social enterprise, Fair Loans intends to make profits and these provide the funds to make grants for community benefit.

⁴⁸ <<http://www.fairloans.org.au/>>.

⁴⁹ Money Fast was the name used for the web-based lender which became Fair Loans Foundation.

4.4.2. CDFI pilot activities

Products/ services developed

Fair Loans Foundation (Fair Loans) offers cash loans of between \$1,000-\$3,000 , for a maximum of 12 months, to people on low incomes whose annual net household income does not exceed \$50,000 (no dependents) or \$60,000 (one or more dependents). Loans are available to Australian citizens and permanent residents over 21 years of age. People in receipt of government benefits are able to apply for loans of up to \$1,000 and those with poor credit history are able to apply if their unpaid defaults total less than \$600.

Loans can be used for any purpose. Where the client has defaults on their credit history, Fair Loans will pay off the default (with funds going direct to the creditor) and the balance is paid into the client's bank account.

Service delivery model

Fair Loans is an internet-based lending institution. Fair Loans developed a cloud-based loan management system that enabled applications to be processed efficiently and automated some aspects of customer assistance. Clients applied online and received an immediate decision on their request, approvals conditional on the successful submission of documentation to prove identity, banking and loans history. Fair Loans committed to providing a loan decision within 48 hours once they received all documentation. Loan decisions were based on bank statements covering the last 3 months. Loans are paid directly into borrowers bank accounts.

Fair Loans also partnered with Corporate Connet.AB to set up a CDFI for the Indigenous community (CDFI.AB) and funded an Indigenous Money Mentor employed by Baptist Community Services in Mount Druitt. This initiative was a result of identifying barriers for Indigenous people to an online model of service delivery. Fair Loans has been exploring working with a community organisation in Penrith to test solutions such as making available a computer kiosk.

Since February 2012 there has been a requirement for all borrowers to contact the Money Mentor before funds are released. The Money Mentor provides assistance by phone and email to clients to explain the terms of the loan and other contract details and, if they wish, to help them prepare personal budgets and to consider strategies to improve their financial situation.

Fair Loans is also exploring the installation of a low cost ATM at the branch with a \$1 fee structure.

Marketing

The website is the main source of enquiries for Fair Loans. Over 3,400 loan enquiries were received via the site to 13 June 2012. The website allows loan applications to be submitted online as well as providing a range of resources to assist people to access financial counselling and links to ASIC's MoneySmart site and other sources of consumer and legal advice.

Fair Loans also report 391 referrals were made by Centrelink and 278 by word of mouth. One hundred and four referrals came from NAB. Advertising was also undertaken, with forty-eight responses to TV and twenty-five to newspaper.

4.4.3. Loan policies/ procedures

Arrears policies

Fair Loans offers clients the option to defer payment if there will not be sufficient funds in their bank account to make their loan repayment on the day which it is due. Fees are charged for a deferral and they are also charged if a direct debit is declined. The arrears policy is applied if a customer misses a single scheduled repayment.

Fair Loans sends the customer

1. An email alerting them they have missed a scheduled repayment
2. An SMS alerting them they have missed a scheduled repayment
3. A phone call alerting them they have missed a scheduled repayment. The phone call also serves the purpose of discovering why the repayment was missed. Fair Loans asks the customer to make the repayment up. If they cannot, notes are made and an agreement to stick to the scheduled repayments is discussed. Repayments may be deferred to be made up at a later date or reduced depending on the client's circumstances.

Fair Loans states that its approach is individual and supportive.

"An understanding and socially responsible approach is taken with each customer on a case by case basis, taking into account their personal circumstances and ability to repay.

If the customer is not contactable and the loan falls into default we use our internal delinquency management procedure which sees the loan fall into our defaulted loans category post 90 days. We do not however default the customer on their credit file until 8 months have passed, providing additional time for the customer bring their facility back in line."⁵⁰

Fees and charges

Fair Loans charges an AAPR of 35 per cent. This means that on a loan of \$1,000, total repayments over 12 months would be \$1,199.50. Repayments are principal and interest, so that the total amount borrowed reduces with each repayment. Repayments can be made weekly, fortnightly or monthly.

There is an establishment fee of \$2.20 and each transaction incurs a fee of \$1.10 (automatically paid to the electronic payments provider). Any failed direct debit payment incurs a \$13 dishonour fee from Fair Loans.⁵¹

Initially, Fair Loans charged a \$50 application fee. This was to be automatically waived for borrowers accessing the Fair Loans Money Mentor, however Fair Loans found that this did not incentivise people to use the service and has since cancelled the fee.

⁵⁰ Fair Loans quarterly report.

⁵¹ These fees do not get paid to Fair Loans and are automatically paid to EziPayment Systems which is a cost of electronic payments.

Compliance issues

During the course of the pilot, Fair Loans informed FaHCSIA that its contract documentation failed to comply with regulatory requirements, specifically relating to accurate representation of the interest rate being charged to clients. As a result, Fair Loans was found to be in breach of the *National Consumer Credit Protection Act 2009*.

In rectifying this, all affected clients were contacted by the Fair Loans' Chief Executive Officer and were repaid any interest erroneously charged. Fair Loans received a financial penalty from ASIC in response to the breach and agreed to engage an independent compliance consultant to report regularly to ASIC.

This issue has highlighted the complexity of the regulatory environment, particularly for small emerging CDFIs operating in the context of new legislation (for example the *Consumer Credit Legislation Amendment (Enhancements) Bill 2012*). It has also raised the need for continued education and monitoring of newly created CDFIs in terms of compliance with relevant legislation. This may include an increased engagement with ASIC to facilitate the identification of compliance issues at an early stage.

4.4.4. Funding

FaHCSIA

FaHCSIA provided \$533,000 (ex-GST) as one-off grant funding to support business development February 2011-June 2012.

Investors — experience

Fair Loans received \$1 million to distribute as loan capital from NAB as an interest-free overdraft. The NAB also supported MoneyFast during the small loans pilot in 2008. The principals of MoneyFast established Fair Loans Foundation as a NFP social enterprise in 2010. They have made personal financial guarantees to back the NAB loan.

Fair Loans has applied for DGR status and hopes to be able to attract philanthropic investment. To date, DGR status has not been secured.

4.4.5. Pilot progress

Number of loans delivered

From the start of the pilot to 13 June a total of 834 loans have been made with a total loan book value of \$2,159,083.

Many people made an initial online application and gained loan approval subject to documentation but did not progress their application. Seven thousand two hundred and eighty-five applications were made resulting in 834 loans. This demonstrates the need for efficient systems and administration to manage the work created by applicants who do not take up loans. The level of interest in the product may also indicate a large number of financially excluded people who are not able to meet Fair Loans criteria or have access to the documentation or technology to complete the process.

The table below summarises the loans made in total by amount. The majority of loans (43 per cent) are for \$1,000, highlighting the need for small amount credit.

Table 21: Fair Loans - loan amount

Loan Amount	Total n	% reported
\$1,000	293	43.4
\$1,500	53	7.3
\$2,000	164	17.8
\$3,000	251	31.5
Not reported	73	
Total	834	100.0

Support services accessed

Six hundred and four people accessed the Money Mentor service overall. For some people this was a short conversation outlining loan conditions. The Money Mentor estimates he had some contact with about 65 per cent of clients, of these about 20 per cent were very engaged and chose to complete budgets and seek feedback, this involved multiple conversations and email exchanges.

Thirty-six per cent of Fair Loans clients are in NSW; 22 per cent in Queensland and almost 19 per cent in Victoria.

Table 22: Fair Loans borrowers by State

State	Borrowers	% reported loans (n=760)
ACT	13	1.7
NSW	300	39.5
NT	8	1.1
QLD	184	24.2
SA	35	4.6
TAS	24	3.2
VIC	154	20.3
WA	42	5.5
Not reported	74	
Total	834	

Client profiles/demographics

The main attributes of Fair Loans clients are summarised in the table below.

Table 23: Fair Loans client profiles

Client characteristic	Total	%
Aboriginal/Torres Strait Island descent	122	14.5
Clients who speak a language other than English at home	Not reported	
Person with a disability	Not reported	
Income under 50k (60k with dependents)	615	82
Male	254	30
Female	512	70 ⁵²
Not reported	68	
Primary source of income – wages full/part time/casual	489	65
Government payments	277	35
Total loans	834	

Since the Indigenous Money Mentor role was established Fair Loans has seen a significant increase in the number of applications from people of Aboriginal and Torres Strait Islander descent, with just two borrowers with loans approved to 14 October 2011, and eighty-eight borrowers in the period 15 October 2011-13 June 2012.

And those refused access?

From the start of the pilot until 13 June 2012, Fair Loans has declined 2,955 applications (44 per cent of applications received). The main reasons applications have been declined are listed in the table below. Fair Loans experiences high numbers of people who make an initial application online but do not proceed with supplying the documentation required to make a loan. These were differentiated for the first time in the January quarterly report where there were 796 incomplete applications.

Table 24: Fair Loans main reason loan declined

Main reason loan declined	Total	% of declined
Customer already overcommitted financially	877	27.7
Unpaid defaults	758	24.0
Negative Uncommitted Weekly Income (UWI) [i.e. customer would be worse off per week with the loan in real \$ terms]	587	18.6
Gambling issues	200	6.3
Bankrupt	114	3.6
Client withdrew	486	15.4
Other	139	4.4
Total declined loans	3161	100.0

⁵² Calculated as a percentage of reported loans (766).

How many people met their loan obligations?

Of the 834 loans, 779 borrowers maintain current repayments (93 per cent) and fifty-five were in arrears (6.6 per cent).

Loan Purpose

The table below summarises the most common reasons why borrowers sought loans in the period 16 August 2011 to 13 June 2012 (data is not supplied for earlier loans and is shown as not reported). Amongst these, the most common reason given for borrowing was to pay bills such as phone and utilities. There were also a large number in the 'other' category.

Table 25: Fair Loans main loan purpose

Purpose of loans	Total loans	%
Pay bills	205	24.6
Buy household item	88	10.6
Holiday	0	0.0
Car rego/repairs	93	11.2
Pay off other credit	25	3.0
Celebration	0	0.0
Education expenses	0	0.0
House repairs	0	0.0
Medical costs	13	1.6
Reduction in income	0	0.0
Start business	0	0.0
Moving house/bond	0	0.0
Other (includes car purchase)	174	20.9
Not reported	236	28.3
Total loans	834	100.0

Case Study

Joe

Joe, who is employed, needed \$2,000 to help cover Christmas expenses. The bank his account is with was unwilling to offer further credit because of previous problems. The Money Mentor comments "Besides a payday lender, this person's only other option was applying for a loan through Fair Loans. Together we filled out the application online, to have it approved later that afternoon. My client is very happy with this outcome, it has boosted their self-esteem, showing that all the hard work in resolving their financial issues over the last twelve months has paid off".

4.5. Community Credit Foundation (CCF)

4.5.1. History and background of the organisation

The Community Credit Foundation (CCF) was established by Fitzroy and Carlton Community Credit Co-operative Ltd (The Co-op) as a vehicle to attract donations and grants to enable microfinance products to be delivered to financially excluded individuals in Melbourne.

The Co-op has been operating for over 34 years, serving disadvantaged communities in inner Melbourne. The Co-op's origins are in the Action Resource Centre Project auspiced by the Brotherhood of St Laurence in 1977. The aim was to provide a savings and loan facility addressing the needs of people on low incomes informed by a commitment to social justice.⁵³ The Co-op currently has 4,800 active members, of whom 3,840 (80 per cent) receive a pension or government benefit.

A key activity for the Co-op has been a budgeting service, which provides individually tailored budgets for members including a special bill-paying service and advice on how to structure bill payments. The Co-op also provides no interest emergency loans for amounts up to \$500, funded by the City of Yarra. Delinquency rates are very low, only \$800 has been written off since the program was established.⁵⁴

According to the Co-op's business case, presented in support of its application to participate in the CDFI pilot, it has always been a strategic objective of the Co-op's to widen its reach to a larger demographic within Australia. This was hampered by the regulatory and capital requirements needed to achieve this. The legal standing of the Co-op as a company, in particular, limited its ability to seek external funding from philanthropic and corporate grants. The creation of a separate foundation, the Community Credit Foundation, was seen as a solution to this problem.

Key benefits to the formation of the Community Credit Foundation included:

- borrowers would not need to be members of the Co-op;
- the entity could seek Deductible Gift Recipient (DGR) status which would then enable funds for loans to be sought through donation and philanthropy rather than member deposits;
- credit union regulations relating to asset holdings and liquidity would not apply;⁵⁵ and
- there could be greater flexibility in considering which clients are eligible and thus more people who experience financial disadvantage could be assisted.

However, as demonstrated by the pilot, it was clearly a complex model to establish.

Organisational structure

The CCF was established as its own legal entity (as a company limited by guarantee) with an independent Board of Directors, governance and reporting framework. Partnerships were developed with local community organisations to facilitate the delivery of programs. While the CCF operated independently of the Co-op, it was able to utilise its relationship with the Co-op to establish products and services targeted at a disadvantaged population, such as using the Co-op's credit license.

The "Call for Expressions of Interest" brochure for Investors (October 2011) detailed the assets, income and expenditure envisaged 2011–14 for the Foundation, working towards full cost recovery

⁵³ <<http://www.fccc.com.au/>>.

⁵⁴ Personal communication from Project Manager 18 June 2012.

⁵⁵ <<http://www.apra.gov.au/adi/PrudentialFramework/Documents/prudential-note-4-1.pdf>>. This note describes the requirements on Co-ops to ensure a minimum amount of funds are readily available to meet the operational and funding needs of the Co-op (both in normal and adverse condition).

within 3 years. This was based on a microfinance loan portfolio of \$1.8 million and administration costs of no more than \$265,000 per annum.

The CCF planned to draw on the experience of the Co-op with a similar approach to the business structures. For example:

- the Co-op makes extensive use of volunteer labour (all the tellers are volunteers) with approximately 10 of 20 staff working in an unpaid capacity;
- the Co-op IT systems could be accessed by the CCF. The system, contains features such as the capacity to set up electronic sub-accounts for individuals for budgeting purposes; and
- comprehensive data is available on cost structures such as how much it costs to process a loan.

Service level agreements between the Co-op and the CCF were proposed to ensure clarity of roles, commitments and relationship but were not completed. They envisaged sharing resources (premises) and services such as loan processing. The business model and relationships between the two organisations were somewhat complex and the regulatory framework appeared to be not well understood.

There have been many challenges for the Board of the Co-op throughout this process and, as at the date of this report, there was still some discussion about the best way to operate. The Chair of the Co-op was acting as Manager of the CCF on a part-time interim basis and consideration was given to integrating the CCF into the Co-op so that was not a separate entity but rather an activity area. This would have a number of implications for the scope of its work and governance. DGR status has recently been granted to the CCF.

A full-time community development manager and a part-time financial literacy coordinator were appointed assisted by an administrator.

4.5.2. CDFI pilot activities

Products/ services developed

The CCF intended developing a range microfinance products similar to those currently offered by the Co-op. These included unsecured personal loans (\$300 to \$1,500 at 13 per cent APR), savings and budget accounts and financial literacy packages.

The financial literacy program was to include financial skills workshops, an outreach budgeting service and the provision of resource packs, as well as referrals to other appropriate support services where necessary. There was extensive consultation with community partners to prioritise issues for inclusion in the Financial Literacy Toolkit which was developed but not implemented.

No products or services were delivered by the CCF during the pilot period. The reasons for this will be discussed in section 4.5.4 below.

Service delivery model

The CCF was to target financially excluded members of the community. It was to operate out of a shopfront in Fitzroy, Melbourne.

There are some concerns relating to the financial literacy model developed. It is based on outreach, but clients would need to visit the Co-op to arrange loans. This may create a complicated pathway and reduce the likelihood of clients following through. A second concern under investigation by the

CCF whether the referring person needs to be an agent of the Co-op because the loans are interest bearing.

Marketing

The CCF has been networking and consulting with local community organisations. A number of agreements have been made with possible partners, such as Good Shepherd Good Money Hubs.

A website was in development: <http://www.communitycredit.org.au/> but was never launched. A DVD was prepared showcasing the positive benefits of financial inclusion using Co-op clients as case studies.

4.5.3. Funding

FaHCSIA

FaHCSIA provided \$300,000 (ex-GST) as one-off grant funding to support business development February 2011–June 2012.

Investors

The Co-op decided when tendering for the pilot not to seek funding from the investment circle, and expressed concern that its independence could be compromised by a relationship with a mainstream bank.

The Co-op's proposed model was based on the investment of capital by organisations that deposit funds on a lower rate of return basis in return for a provision of services offered to disadvantaged people. A potential key target for these donations was the Credit Union movement and superannuation funds as well as trusts and foundations. Formal proposals were presented to potential supporters. For example, the CCF produced a "Call for Expressions of Interest" brochure inviting support from philanthropic and corporate partners, first released at the ABACUS Convention in October 2011. The CCF sought support from partners to build a \$1.8 million portfolio by 2014 with initial contributions up to \$200,000 in the form of grants, donations or interest free loans.

In order to support this, the CCF sought to acquire DGR status through the Australian Taxation Office. It was hoped that this would enable it to raise donations and create a pool of capital for lending. The length of time this has taken has impacted on progress with the acquisition of capital. This lack of loan capital delayed the commencement of lending and the CCF had not made any loans by the end of the pilot period.

To date there is little evidence that this initiative has been successful in securing corporate deposits into the CCF. We were advised that one corporate sponsor may have offered a grant of \$25,000 to the CCF to fund interest free emergency loans, however, the status of the donation is currently unclear.

As an authorised deposit-taking institution, another major source of capital for the CCF was to be through deposits made to the Co-op. In particular, the Co-op has an arrangement with 40-50 locally-based community sector organisations who bank their grants with the credit union. It was proposed that the revenue stream from earnings on these deposits would be redirected to the costs of providing the credit union services to people on a low income. This turned out to be quite problematic as this exposed the Co-op to capital adequacy issues and was not pursued.

4.5.4. Discussion — learning from the pilot

The CCF was not able to commence lending during the pilot period. WWS has met with the Chair of the Co-op and the CCF managers to discuss and identify some of the main reasons why it has not been possible to achieve the workplan envisaged when the pilot contract was agreed.

Tracking the number of different business plans developed (five) is one indicator of the lack of clear direction and agreement at a senior level about the role and activities of the Co-op. Significant differences in direction include:

- which organisation (Co-op or CCF) would write loans— at one point during the pilot the Board of the Co-op determined that the role of the CCF would be to make referrals to the Co-op rather than lending itself; and
- which organisation would manage the City of Yarra emergency loans program — approval was sought for the CCF to do this rather than the Co-op and the City of Yarra agreed, however, the Co-op Board decided not to proceed.

Some of the factors contributing to this were:

- new Board members at the Co-op who had not been involved in early discussions and did not own the innovation;
- a lack of stability in the membership of the Board of the CCF;
- changes in management at both the Co-op and Foundation and a lack of senior management capacity (working just one day a week) to navigate the range of political and practical issues involved in innovating on this scale for the Co-op and support the Community Development Manager;
- while staff working on setting up the Foundation were able to identify actions required and develop proposals, the Board of the Co-op could not keep pace, described as “one side with a foot on the accelerator whilst the other was pressing on the brake”. With hindsight, the Co-op may have been reluctant to relinquish control to the Board of the CCF and unaware of potential impacts on the Co-op of the initiative when tendering for the pilot; and
- The CCF had limited resources for the pilot and worked in office space also required by the Co-op for meetings.

No capital funding was secured and the pilot may demonstrate the challenges of the “grants culture” identified by Burkett (2010).

Jones and Goggin (2007) researching the development needs of UK credit unions and CDFIs found that a priority need was training to strengthen boards of directors, and their findings may also be relevant to the experience of the Co-op.

5. Survey Responses

The evaluation included two surveys designed to hear directly from borrowers about their experiences in taking a loan from one of the CDFI pilot lenders.

An initial (baseline) survey sought to understand some of the demographic characteristics of borrowers, some insights into their current financial circumstances and the purpose for which they were seeking a loan at the time the loan was being processed. A follow-up survey re-visited a number of questions such as loan purpose, current savings and budgeting patterns, strategies for dealing with shortages of money, measures of financial confidence and satisfaction with financial situation. Demographic characteristics of borrowers were also rechecked. This survey collected views from borrowers after their loan had been in place for a number of months. All follow-up respondents were still paying off their loan at the time of the follow-up survey. Questions were asked about satisfaction with price of loan, ease of loan repayment, participation in financial education and impact of loan on financial stress.

5.1. Response rates

There were 42 new clients who responded to the initial online and paper survey. WestWood Spice had requested all CDFIs in the pilot to invite all new clients to respond. Responses were received from all four of the pilots lending to clients. As a proportion of loans written, these response rates were low. The survey methods were selected and approved based on the anticipated loan numbers in the CDFI workplans. Other studies have also found it challenging to get participation from similar client groups on this topic as people can feel embarrassed talking about financial problems (NAB 2010; Wesley Mission 2010; Banks et al. 2012).

For the follow-up survey, there was information in respect of 16 clients. Three of these had responded directly online to the follow-up survey. The remainder had indicated that they were happy to be contacted by telephone and the survey was completed as a telephone interview with these clients. Clients providing follow-up information were connected to three of the five CDFI providers. In-roads operates as a partnership program with seven non-government organisations, and their participating clients were linked to the relevant partner.

The distribution of survey responses across the programs was as follows:

Table 26: Distribution of initial survey responses

Program	First Survey Response Rate		Follow-up Survey Response Rate		Loans written
	#	%	#	%	
In-roads (Community Sector Banking)	14	33%	7	43%	158
Fair Loans	10	24%	1	6%	746
Fair Finance Australia (Foresters)	11	26%	8	50%	61
Many Rivers Microfinance	7	17%	0	0%	122
TOTAL	42	100%	16	100%	1087

5.2. Client Demographics

Client's experience

"I am a single parent on disability. This loan allowed my daughter and I the freedom to choose a healthier lifestyle. Not only has my medical condition improved dramatically, but my daughter is flourishing in our new rural environment. Thanks to this move, I also have the peace of mind, and health, to have enrolled to study for a degree. I would never have been able to do this, had I not had access to this loan. It is a terrible shame that so few of these institutions are available to lower income earners, and even more of a shame, that very few people know of their existence. I made hundreds of telephone calls, over an entire month, before I was given the contact information of this particular financial institution. My only gripe is that the interest rate is quite high! However, our future is much brighter thanks to these financial services."

Survey response 16

Both the initial and follow-up surveys asked respondents to provide a number of demographic details about themselves.

The typical respondent to the initial survey was likely mid-30s, female, non-Indigenous, likely to have completed Year 12 and be a single or sole parent, renting and in receipt of some form of government benefit, with average weekly net income between \$400 and \$599. The profile of Fair Loans clients is somewhat different: on the whole they are a younger age group of clients, and there is a much higher proportion of couples (40 per cent versus 17 per cent).

5.2.1. Residential Status

The vast majority of all the borrowers who responded to the initial survey (78 per cent for Fair Loans and 94 per cent for the remainder) were living in rented accommodation. For the follow-up survey 88 per cent were living in rented accommodation. This was split equally between public and private rentals. One person was living with their family and one person was house-sitting. There were no property owners.

5.2.2. Net weekly income

The majority of respondents provided information about their income level after tax was taken out. The follow-up sample had a larger proportion of people in the lower income group, with 86 per cent of people under \$600 per week. The major source of income for survey respondents was a government pension or allowance (61 per cent), with most of those either on a parenting or carer payment (42 per cent) or a disability support pension (37 per cent). A total of 39 per cent of respondents listed their main source of income as a wage or were self-employed.

5.2.3. Aboriginal or Torres Strait Islander descent

While the Indigenous proportion of the initial sample was in the minority, at 36 per cent, this is significantly higher than the Australian population percentage of Indigenous and Torres Strait Islander people (2.5 per cent at 2006 ABS Census).

5.3. Financial Stress

In both surveys, a little over half of respondents provided information about their responses to a series of questions relating to financial stress in the past 6 months, with some respondents giving more than one response. There is a significant difference in the pattern of responses between the initial and follow-up surveys, though the small sample size of the latter should be kept in mind. The telephone interview format may also have made it easier for people to disclose past difficulties. The picture which presents is one of considerable financial hardship with a high reliance on alternative forms of lending such as payday lenders. People also mentioned making use of food vouchers, food bank and free meals.

Table 27: Responses to money shortages

Responses to money shortages	Respondents from initial survey (n=24)		Follow-up respondents (n=8)	
	#	% ⁵⁶	#	%
Could not pay electricity, gas or telephone bills on time	8	33%	6	75%
Could not pay the rent or mortgage on time	4	17%	1	13%
Pawned or sold something	5	21%	2	25%
Went without meals	2	8%	4	50%
Was unable to heat home	0	0	1	13%
Asked for financial help from family or friends	10	42%	2	25%
Asked for financial help from a welfare or community organisation	4	17%	4	50%
Approached a payday lender	3	13%	5	63%

Respondents were asked to rate their overall satisfaction with their financial status on a 10 point scale, ranging from 0 (completely dissatisfied) through to 10 (completely satisfied). The average response was 7.88 and 40 per cent gave themselves a rating of ten. Without a previous baseline measure, it is difficult to determine if the impact of having just secured a loan had a positive effect on the rating. However, the average had dropped to 6.86 in the follow-up survey. There was still a similarly high proportion of people rating nine or ten (44 per cent versus 45 per cent), but this was counterbalanced by a few people who rated at the dissatisfied end of the scale. Again, the small sample size means caution in interpreting these results.

Despite these figures, two-thirds of follow-up respondents reported that the loan had made an impact in reducing their financial stress levels.

“I missed a payment — asked for leeway — they added it to the end of the loan. If I can pay off faster the loan will reduce.”

Survey response 4

⁵⁶ Some respondents gave more than one response.

5.4. Client Loan History

There were a number of questions in the survey designed to provide a picture of the previous loan histories of borrowers. Respondents were asked whether they had any other current loans and whether they had borrowed money in the past. Two-thirds of borrowers indicated that they did not have any other current loans, whilst one-third did have another current loan.

5.4.1. Source of previous loans

For the respondents from three of the CDFIs, the most common source of previous borrowing had been Centrelink advance payments. Approximately one-third of previous borrowers had a loan from a bank or credit union, but there were similar numbers who had sourced loans from either payday lenders or pawn brokers. Another 22 per cent had borrowed from a finance company. While responses from Fair Loans clients also indicated a high proportion of Centrelink advances, there were also higher levels of borrowing from finance companies amongst this group (although it should be noted that the sample size is very small). Details are provided below.

Table 28: Source of previous loan

Source of previous loan (indicating all that apply)	Respondents – Many Rivers, Fair Finance and In-roads		Fair Loans	
	#	% ⁵⁷	#	%
Loan from family/ friend	5	18%	1	11.1%
Centrelink Advance payment	17	61%	6	66.7%
Loan from Bank/ Credit union	9	32%	4	44.4%
Credit Card	4	14%	3	33.3%
Finance Company	6	22%	6	66.7%
Payday lender/ Pawn Broker	9	32%	1	11.1%
Community Service provider e.g. NILS®	2	7%	0	0.0%
TOTAL # of clients providing information	28 clients		9 clients	

5.4.2. Previous loan attempts

One-third of initial respondents indicated that they had tried to get a loan elsewhere prior to applying for their current CDFI loan. Information on who had been approached was available for most of these people (n=12). This showed that two-thirds had approached banks (one for a credit card), there had been one approach to Cash Converters, one to Rapid Car Finance and the remainder had sought a loan from a credit union. Among those who had sought a loan elsewhere, the majority had looked to mainstream financial sources.

In most cases, the outcome of this other loan application was that the person was not offered a loan (83 per cent). One person was offered a loan and took it. One person was offered another loan, but chose not to take it. In this instance, the person had approached Cash Converters.

Over half of respondents had the experience of having previously applied for a loan and being rejected.

⁵⁷ As some respondents had more than one previous loan, percentages do not sum 100.

Among those who had not previously had a loan, one-third indicated that this was because they had not needed a loan until now. However, 50 per cent indicated that they did not think they would get a loan because of their situation. Two people indicated that they had had a previous default/bad credit history. One person said that they had been rejected by a bank/credit union and one person indicated that they did not like being in debt.

5.5. Client Experience with the CDFI

5.5.1. Finding CDFI providers

Respondents were asked how they had found out about the CDFI organisation which supplied their loan. The most common method was through a local charity or community service, with slightly under half of respondents (43 per cent) indicating this method. A number of people provided details of the specific organisation which was involved. The next most common method was family and/or friends with 14 per cent in this group. Other methods included government sources other than Centrelink (10 per cent), the internet (21 per cent of responses) and newspaper or magazine advertising (5 per cent), with one person finding out from a bank/credit union and one person from a community radio station interview. For Fair Loans clients, the internet was the primary method for 78 per cent of those responding.

5.6. CDFI loan

Eighty-five per cent of initial respondents supplied information about the amount they had borrowed from their CDFI. The highest amount borrowed was \$17,000 (this was a Many Rivers client) and the lowest was \$1,000 with an average of \$3,254. The most common amount was in the range \$1,000 to \$2,000. In five instances, loan amounts were listed to the last 'dollar and cent'. This indicates very clear transparency about the total amount being borrowed, inclusive of interest. In all instances these borrowers were customers of Fair Finance.

All but one of the baseline respondents provided information about the purpose of their loan. In the case of Fair Loans, the most common loan purpose was to pay bills (50 per cent of respondents), followed by car registration/repairs. One person used their loan for medical/dental costs and one person said 'Christmas shopping'.

For the other providers, the most common purposes were either car related (37 per cent were either buying a car or paying for car registration/repairs) and 32 per cent of loans were for business purposes, with about half of the business loans involving the starting of a business and the other half relating to an existing business or business expansion. Paying bills and debt consolidation were the next most common category (24 per cent) with two loans for education and/or training expenses and one for purchase of a household item, for example whitegoods or furniture.

With no Many Rivers clients in the follow-up survey and therefore no loans for business purposes, the most common purposes were equally split at 33.3 per cent between car-related (either buying a car or paying for car registration/repairs) or paying bills and debt consolidation. Holiday spending, house repairs and funeral expenses were also mentioned.

It is interesting to note the incidence of lending for bill paying and debt consolidation which account for a sizable minority of loans and are areas of lending which are often not permissible under other forms of credit accessible by people who are financially excluded, such as NILS loans.

5.6.1. Loan repayments

Interest rate

Follow-up survey respondents were asked to indicate what interest rate they were being charged on their loan. The majority were able to provide the rate correctly, indicating the transparency of the loan. These results are shown below.

A follow-up question asked: Do you believe that this loan is reasonably priced compared to other similar loans? Across all respondents, seven out of thirteen said “Yes”. However, when this question was cross-tabulated with the interest rate being charged on the loan, all the people who had nominated 34 per cent or 35 per cent said “No”, that the loan was not reasonably priced.

“If I had a choice of Financial Institutions, I would prefer one that had a much lower interest rate. It is the only concern I have about the entire process.”

Survey response 15

Loan repayments

Thirteen respondents answered the question: “Are you on track for paying off your loan according to the terms of your loan agreement?” and all of these answered in the affirmative. A supplementary question asked whether the loan had been difficult to repay. One person said “Yes”.

Future borrowing

The question was posed: “If you needed another loan, where would you go to get it?” All except one borrower said that they would go to the same provider who gave them their current loan. This person said they would seek a Centrelink advance.

“At the end of the day I now have a car - Money is tight but gee it is worth it.”

Survey response 6

5.6.2. Client satisfaction with CDFI

Both initial and follow-up survey respondents were asked to indicate on a 10 point scale how likely they would be to recommend this loan to friends or family. Over 83 per cent of initial respondents rated nine or ten — that they would be extremely likely to recommend the loan (78 per cent rating ten). Ten per cent were neutral (rated five). Results were almost identical amongst follow-up respondents with 83 per cent of respondents rating a nine or ten. Eight was the lowest rating. This indicates a strong support for the loan product.

Eighty-six per cent of initial respondents indicated that their loan was “exactly what I was looking for”. Three clients indicated that they would have preferred a larger loan amount (these were all Fair Loans clients), and there were three respondents who indicated that they would have preferred a longer loan term. In two of these cases these were clients with larger loans which were for business purposes (\$10,000 and \$8,900 respectively) each of which had a 12-month term.

Three-quarters of the baseline survey respondents gave a response to the question; “What do you like most about the loan?” There were five clusters of responses. These are shown in the table below, together with some examples of comments made in each category.

Table 29: Client views on loan

What do you like most about the loan?	Examples of responses	(some people mentioned several aspects of the loan)
	# of respondents	Comments
1. Characteristics of the Loan	14	<p><i>“The payment terms are very reasonable and the interest is variable”</i></p> <p><i>“There is no penalty if you have a temporary setback”</i></p> <p><i>“Flexibility”</i></p> <p><i>“No extra charges”</i></p>
2. Customer service	8	<p><i>“No judgment and given a fair go”</i></p> <p><i>“Personal service and able to contact provider”</i></p> <p><i>“The staff are compassionate and helpful and make you feel worthwhile, just in a bad spot”</i></p> <p><i>“Understanding and easy to talk to”</i></p>
3. Impact on financial circumstances	6	<p><i>“Help to get my life on track”</i></p> <p><i>“Fairness for the low income and struggling Aussies”</i></p> <p><i>“It enabled me to avoid a financial disaster and get back on my feet again financially”</i></p> <p><i>“Starting my credit rating”</i></p>
4. Benefits due to loan purpose	4	<p><i>“Support given for business mentoring”</i></p> <p><i>“The ability to now undertake study”</i></p>
5. Method of securing loan and repaying loan		<p><i>“That the loan was available online and over the phone, easy to set up, easy to understand and that there was a financial assistant available and that the loan comes straight out of a bank account”</i></p> <p><i>“Payment plan is direct debited out of my account, it’s easy to manage, and Fair Loans are easy to deal with”</i></p> <p><i>“It was quick and easy”.</i></p>

5.6.3. Suggestions to improve the loan

The most common suggestions were to reduce the interest rate. Others mentioned the need for increased publicity so that others knew about the product, and some were doing their own informal recommendations. There was also positive feedback about helpful loans officers.

There was support for the current practice of most of the CDFI providers to pay the money advanced to the third party supplier of goods or services and the ease of direct debits to repay was also highlighted.

5.7. Capability Building

5.7.1. Saving and Budgeting

Both baseline and follow-up survey respondents were asked to describe their savings pattern. The most common response amongst the initial survey respondents was: “I save the odd amount when I can” (42 per cent) with another 32 per cent indicating that they “regularly save what is left over after other expenses”. Interestingly, a higher proportion of follow-up respondents indicated that they did not save anything (46 per cent compared to 17 per cent). This may reflect that the securing of a loan had impacted negatively on their ability to save. With respect to use of a household budget, there was a higher proportion of respondents in the follow-up who were using budgeting (72 per cent compared to 55 per cent).

Responses across both surveys are shown below.

Table 30: Saving and budget habits

Savings pattern	Respondents (initial survey)		Respondents (follow-up survey)	
	#	%	#	%
Save a set amount on a regular basis	6	15%	1	8%
Save what is left over after other expenses	11	27%	2	15%
Save the odd amount when I can	17	41%	4	31%
Don't save anything	7	17%	6	46%
TOTAL	41	100%	13	100%

Table 31: Use of a household budget

Use of a household budget	Respondents (initial survey)		Respondents (follow-up survey)	
	#	%	#	%
Never	3	7%	1	14%
Sometimes	16	38%	1	14%
Regularly	10	24%	2	29%
Always	13	31%	3	43%
TOTAL	42	100%	7	100%

5.7.2. Financial education

Follow-up respondents were also asked if they had participated in any financial education.

A little over half the respondents (54 per cent) indicated that there had been financial training or financial counselling associated with their loan. Of these, 83 per cent said that it had been helpful. The most common reason selected by those who were asked to say why they had not received financial training or counselling was: “I didn't need it because I know enough about managing money”.

5.7.3. Confidence in managing money

Sixty per cent of follow-up respondents indicated that they feel more confident managing money than before, with the remaining 40 per cent rating their confidence levels the same as before.

Respondents were also asked to indicate any other differences which having the loan had made. A number mentioned having been rejected by banks for a loan and how useful having the loan had been. Others mentioned the benefits of having a car where this had been the loan purpose.

6. Results

6.1. Overview

Section 6 considers what has been achieved and what can be learnt from the pilot to date. It addresses the key evaluation questions by using a results based accountability framework (Friedman 2005), drawing attention to four areas of performance results:

- Quantity: how much did we do?;
- Quality: how well did we do it?;
- Effort: how hard did we try?; and
- Effect: what change did we produce?

These performance results were used to address the three key evaluation questions:

- A. How effective were the CDFIs in increasing the ability of disadvantaged individuals to gain access to appropriate credit?
- B. Was the demand for appropriate financial products and services best met by CDFIs?
- C. What mechanisms and barriers did the CDFIs face in gaining access to capital?

Detailed questions were developed to investigate the performance of the CDFIs (see Table 35).

Table 32: List of investigative questions

Investigative questions addressed in the report	Key Evaluation question
Quantity	
▪ What types of financial products/ services have been developed? What services other than loans are offered (e.g. business planning, financial counselling)?	A
▪ How have products been distributed/ marketed?	A
▪ What was the take up by clients?	A
▪ What was the CDFI contribution in meeting demand compared with other loan products?	B
▪ What was the relative cost to government?	B
▪ How much capital funding was achieved?	C
Quality	
▪ What was the profile of clients accessing products/ services?	A
▪ How did the CDFIs engage with clients?	A
▪ What was the client view/ experience of the product?	A
▪ What was the experience of CDFIs in working with investors?	C
Effort	
▪ What factors influenced any variations in results between pilot organisations?	A
Effect	
▪ What were the outcomes for clients?	A
▪ How many people met their loan obligations?	A
▪ What were the outcomes for CDFIs?	B
▪ Was there a community level impact from CDFIs?	B
▪ Was the demand for financial products and services best met by CDFIs?	B
▪ Was the financial model sustainable?	B

6.2. Quantity—how much did we do?

6.2.1. What types of products and services have been developed?

The four active CDFIs developed a range of financial products and services. These are listed in the table below.

Table 33: Products and services developed by CDFIs

	Product	Service	Outputs		
			# loans	Loan book value \$ (at 13 June 2012)	Support (e.g. money mentor, business planning) # people
In-roads (Community Sector Banking)	Personal loans \$500-\$3,000 unsecured 24month term	Financial education Credit history information Assistance with debt renegotiation Referral to other support agencies	158	423,180	158
Fair Finance	Personal loans \$1,000-\$4,000 (flexible) unsecured 12-24month term	Financial education Credit history information Assistance with debt renegotiation Referral to other support agencies NILS	61	164,402	122
Fair Loans	Personal loans \$1,000-\$3,000 unsecured 12 month term	Money Mentor offers telephone and email support with budget development Indigenous Money Mentor offers face to face support with loan applications in Penrith/Blacktown Website has resources (e.g. budget planner, information for debtors, Understanding money website).	834	1,571,500	604
Many Rivers	Small business loans \$500-\$20,000 unsecured 6month-3year term	Enterprise support, business coaching and skill development including bookkeeping and financial literacy	122	668,545	367

6.2.2. How have products been distributed/ marketed?

Each of the pilot organisations undertook a variety of marketing strategies. Word of mouth was reported to be the most effective mechanism, particularly for Indigenous people. Collaboration with other community groups and agencies working with low income clients such as employment networks was also found to be effective. The link between Parklea Prison and Many Rivers is an example of this.

One challenge experienced by CDFIs in building awareness of their work was the reluctance of some in the community sector to refer clients to CDFIs because of their interest-bearing nature. There was also concern expressed among the CDFIs that accessing the target market of “the working poor” is a significant challenge. This will require development of different referral channels from those traditionally used by CDFIs. Efforts to explore alternative options were restricted by the limited timeframe of the pilot. In some regions, banks, especially NAB and Bendigo Bank, were reported to be making referrals. Many Rivers was also able to use Westpac branches as bases in some locations.

All of the CDFIs except the CCF developed a website. The internet has been particularly important for Fair Loans as its primary source of clients. Many Rivers and In-roads created promotional DVDs with client case studies.

6.2.3. What was the take up by clients?

Across the four lending CDFIs, there was a total loan book value of \$2,827,628 as at the end of the last reporting period (13 June 2012). This comprised micro credit of \$668,545 supporting 122 new businesses by Many Rivers and 1,053 personal loans totalling \$2,159,082.91.

A total of 367 people accessed business planning support and 1,093 accessed financial literacy support or money mentoring.

Most personal loans were in the \$1,000-\$3,000 range for terms of 12 months to two years. The main loan purposes were to pay bills, register or repair cars and pay off other credit. A total of 86 loans to individuals for enterprise start-ups were in excess of \$4,500.

6.2.4. What was the CDFI contribution in meeting demand compared with other loan products?

Table 35 summarises some of the different products available to people on low incomes including two payday web based loan products.

Eligibility

All of the products are available to people on low incomes and with poor credit histories. NILS and StepUP require people to hold a concession card.

The eligibility criteria for the In-roads product are very similar to the StepUP loans and it is likely that they have been most popular in areas where StepUP is not readily available. CDFIs are lending to people with slightly higher levels of loan defaults.

Length of time to receive funds

Compared with NILS and StepUP, the CDFI loan process is typically faster. The implementation of NILS varies between states and organisations, but may rely on a volunteer committee meeting monthly, for example. StepUP requires an appointment with a microfinance worker and then assessment by NAB. This takes about five days following the appointment.

Payday lenders' websites claim to offer decision making and transfer of funds of 24 hours or less. CDFIs are slower. Some of the reasons for this include setting up face-to-face appointments, ensuring clients have adequate documentation to support their application, and delays in securing supplier information. Loans related to car purchase or repair were particularly slow as a borrower might spend some time sourcing a vehicle or obtaining a quote once a loan had been agreed in principle. In remote areas finding suppliers to deliver to clients was also problematic.

Loan amounts

Payday lenders offer small amounts — \$50 for example — for terms as short as eight days as well as larger amount for longer terms. None of the CDFIs offered an equivalent product. Fair Finance was the only CDFI with the flexibility to make a loan of less than \$1,000 (3 instances) and also offered terms of less than one year.

"I've been with my own bank for 55 years. I went to ask them for a loan and they said "No, I couldn't have \$2,000 but I could have \$5,000". Someone at NAB told me about Fair Finance. I borrowed just under \$3,000 to get my car repaired and to pay off other credit. I am going to pay \$150 for 12 months rather than \$132 to get it paid faster. The loan made all the difference in the world to me."

Survey response 5

Loan purposes

Fair Finance and In-roads make payment to suppliers in the same way that NILS and StepUP do. In this fashion loans are limited to specific purposes and they cannot be used for day to day expenses. Fair Loans and the two payday examples deposit funds into a borrower's bank account and these can be used for any purpose.

CDFIs are assisting people with debt consolidation and this is not possible using NILS or StepUP loans.

Other services

NILS, StepUP and CDFIs all offer support to borrowers, assisting them to prepare budgets, understand their finances and repair credit histories where possible. One In-roads relationship manager commented "Financial literacy starts the minute they walk through the door".

Table 34: Different loan types

	NILS	STEPUP	IN ROADS	FAIR FINANCE	FAIR LOANS	PAYDAY – ALLSTAR *	PAYDAY – CASH DOCTORS*
Who can apply?	<ul style="list-style-type: none"> • Centrelink Healthcare or Pension Card holders or eligibility to receive Family Tax Benefit Part A • Must have lived at their current address for more than three months (exceptions available) 	<ul style="list-style-type: none"> • Centrelink Healthcare or Pension Card holders or eligibility to receive Family Tax Benefit Part A • Must have lived at their current address for more than three months (exceptions available) • Debts less than \$500 	<ul style="list-style-type: none"> • Australian citizen or perm. resident • 18 years or over • Annual household income less than \$50,000 (gross) • Centrelink Healthcare or Pension Card holders or eligibility to receive Family Tax Benefit Part A • Demonstrated ability to make regular payments • Current address for six months 	<ul style="list-style-type: none"> • Australian citizen or perm. resident • 18 years or over • Anyone financially excluded • Demonstrated ability to make regular payments 	<ul style="list-style-type: none"> • Australian citizen or perm. resident • 21 years or over • Annual Net Household income must not exceed \$50,000 (no dependents) • \$60,000 (one or more dependents) • Unpaid defaults of \$600 or less 	<ul style="list-style-type: none"> • Full or part time employment (4 months in current job) or regular Centrelink payment • Email account or access to fax machine 	<ul style="list-style-type: none"> • Full or part time employment (Centrelink beneficiaries not eligible if primary source of income) • Borrowers become members, funds accessible 24/7
Speed of Process	<ul style="list-style-type: none"> • Process varies in each state, may take up to 4–6 weeks 	<ul style="list-style-type: none"> • Appointment with Microfinance worker then application assessed by NAB (about 5 days for NAB assessment) 	<ul style="list-style-type: none"> • Initial assessment (in person, by phone or online). • Face-to-face interview with relationship manager • Process can be same day if all documentation available, average 6 days 	<ul style="list-style-type: none"> • Initial assessment (in person, by phone or online). May refer at this point if another agency is more suitable. • Face-to-face interview • Process can be same day if all documentation available, usual wait time is 1.3 days for decision, 2.43 days for funds 	<ul style="list-style-type: none"> • Online application , conditional approval in 5 minutes • Applicant then needs to supply documentation , decision promised in 48 hours once all docs received • Money mentor appointment made before funds issued. 	<ul style="list-style-type: none"> • Online approval within hours • Cash in account the following day 	<ul style="list-style-type: none"> • Online . • Automatic approval and credit check • Employment details checked with payroll by phone (or post) • Funds transferred within 60 minutes of approval
Min/max \$	200–1,500	800–3,000	500–3,000	1,000–4,000 (flexible)	1,000–3,000	50–500	220–600
Credit check	X	X	✓	✓	✓	X	✓
Terms	Nil interest	3.99% APR 6month-3year term	13.95% APR 12 – 24 months	35% APR 12 – 24 months (flexible)	35% APR 12 month	\$10 per \$50 borrowed per fortnight	\$45 draw down fee \$30 per week 45 day term
Payment method	Cheque to trader	Cheque to trader	Cheque to trader	Cheque to trader	Money into bank account/default is paid to creditor	Money into bank account	Money into bank account
Loan purpose	<ul style="list-style-type: none"> • white goods • furniture • medical • education 	<ul style="list-style-type: none"> • white goods • furniture • education • car 	<ul style="list-style-type: none"> • Any legitimate purpose except day to day expenses. Debt consolidation 	<ul style="list-style-type: none"> • Any legitimate purpose except day to day expenses • Debt consolidation 	Any	Any	Any
Financial literacy training	✓	✓	✓	✓	✓	X	X

* Data from websites < <http://www.allstarpaydayloans.com.au/>> < <http://www.cashdoctors.com.au/>> accessed June 2012

6.2.5. What was the relative cost to government?

The five CDFIs were funded for organisational development. The total investment was \$6,029,000 by Government. Complementary initiatives relate to financial counselling and NILS. In 2011-12, nearly 100 community and local government organisations received funding totalling around \$15.3 million to deliver Commonwealth Financial Counselling face-to-face services across Australia.⁵⁸ In 2009 and in 2011, the Australian Government funded GSYFS to fund NILS and StepUP loans. Total government funding of these initiatives is \$36.4 million with provision in the budgets 2009-10 to 2013-14.

Table 35: Government Funding

	Many Rivers	Fair Finance	In-roads	Fair Loans	FCCC	Total
Government funding	\$986,000	\$2,040,000	\$2,170,000	\$533,000	\$300,000	\$6,029,000

6.2.6. How much capital funding was achieved?

The CDFIs all sourced capital in different ways. The table below summarises the sources of capital and arrangements for lending. Progress has not yet been made in establishing a corpus of funds earning interest to create income streams for CDFIs.

Table 36: Capital funding

	Many Rivers	Fair Finance	In-roads	Fair Loans	FCCC
Capital funding	—	\$1,000,000	\$1,000,000	\$1,000,000	— ⁵⁹
Source	Westpac	NAB	Bendigo	NAB	—
Nature	Lends off the Westpac balance sheet	Interest free overdraft	1,000,000 allocated for In-roads lending from balance sheet. CSB reserves \$200,000 to take first loss risk	Interest free overdraft	

6.3. Quality - How well did we do it?

6.3.1. What was the profile of clients accessing products/ services?

CDFIs had performance indicators to ensure that 95 per cent of their clients were from target groups which included people on low incomes, Indigenous Australians, people with a disability and people who speak a language other than English at home (see Table 40). Fair Loans and In-roads restricted access to their products to people from the target groups, and the requirement to have an annual household income of less than \$50,000 (\$60,000 with dependents for Fair Loans) was publicised. Fair Finance did not apply such criteria, preferring to use the screening interview to determine financial exclusion and refer elsewhere if an applicant would be able to access mainstream lenders. About a third of In-roads and Fair Finance clients were people with a disability. Many Rivers targeted its activities in areas of disadvantage and only worked with clients unable to access other supports.

⁵⁸ <<http://families.fahcsia.gov.au/our-responsibilities/families-and-children/programs-services/commonwealth-financial-counselling-cfc>> accessed 19 June 2012.

⁵⁹ WestWood Spice understands that CCF may have been successful in an application for grant funding for emergency loans however this funding is not available to use as capital for interest bearing loans.

None of the CDFIs reported significant proportions of clients who spoke a language other than English at home, although In-roads-CAIE in Ipswich was in the process of developing a partnership with a refugee organisation.

Almost 30 per cent of borrowers across the four CDFIs identified as Aboriginal or Torres Strait Islander. The proportion was highest for In-roads (64 per cent) and lowest for Fair Finance (8 per cent). A third more women than men took out personal loans, however, more men than women received enterprise support through Many Rivers. Over a third of Fair Finance and In-roads' clients reported having a disability. Fair Loans was the only organisation to have a majority of clients with wages rather than government payments as their primary source of income (65 per cent).

Table 37: Proportion of clients from target group

	Many Rivers	In-roads	Fair Finance	Fair Loans	Total
Indigenous Australians	107 (75%)	101 (64%)	5 (8%)	122 (14.5%)	335 (28.5%)
Clients who speak a language other than English at home	1	1	4	-	6
Person with a disability	-	57 (36%)	21 (34.4%)	-	
Income under 50k	104 (73%)	158 (100%)	32 (52%)	615 (82%)	909 (77%)

6.3.2. How did the CDFIs engage with clients?

Within these basic products and services, the CDFIs have differed dramatically in their service delivery model, particularly in the intensity of engagement with the client. Understanding the intensity of engagement is significant because addressing financial exclusion is not simply about the delivery of loans. Any attempt to address financial inclusion must also reflect the assistance provided to people for whom it may be inappropriate to lend money to, but who may derive benefit from their interaction with the CDFI nonetheless.

The Fair Finance and In-Roads models, for example, offered intensive, face-to-face budget review and support processes alongside the loan application process and during the term of the loan. Both organisations reported that this face-to-face input was more effective than offering group training sessions in financial literacy. In both these models, staff were available for clients to contact if they had any problems with repayments or other issues associated with the loan. For Many Rivers, assistance to help people establish or expand a business may take several months if not years, and the support of field officers was available from the earliest stages of developing an aspiration to be self-employed, through the preparation of a business plan and into the first years of trading. Of all the four models, Many Rivers provided the most intense engagement with the client.

All three of these CDFI models provided support to significant numbers of people who did not end up with a loan but benefited in other ways, such as through assistance in the preparation of a budget, intervention with debt issues, introduction to other agencies or clarification of personal goals.

The least intensive model of the four was Fair Loans. The Fair Loans Money Mentor had limited contact with clients during the first months of the pilot. Contact was voluntary although incentivised. From February 2012, a new arrangement was made whereby clients were required to contact the Money Mentor before loan funds were released.

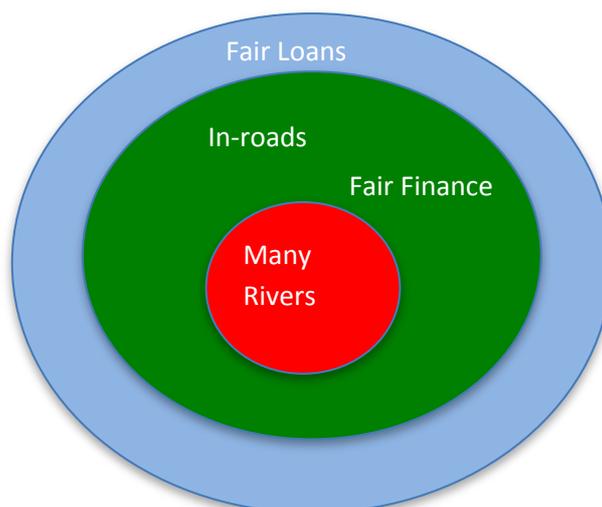


Figure 2: Intensity of client engagement

This resulted in a dramatic increase in the number of phone or email contact with clients. Overall, about a fifth of Fair Loans’ clients received assistance with the preparation of a financial budget. This is a very different intensity of support from that offered by the other personal lenders in the pilot and positive feedback was reported from those clients who took advantage of the service. However, applicants who were not approved for loans did not receive any service or referral. Through the Indigenous Money Mentor a case-based service was offered to a small number of clients. Should Fair Loans develop their proposed branch model, applicants as well as borrowers will have access to this support.

The different models of service engagement have been represented using an ‘intensity’ target (see Figure 3). The CDFI who engaged in the most intense engagement with the client is shown at the centre of the target and the least at the fringe.

6.3.3. What was the client view/experience of the product?

Feedback from the survey and interviews with clients and CDFI staff indicates increases in confidence and self-esteem attributed to having been deemed credit worthy and successfully making loan repayments: this is consistent with the findings of Proske (2010) and Corrie (2011) relating to NILS and other credit programs for people on low incomes.

Clients surveyed were very positive about the scheme, with over 90 per cent stating they would recommend their CDFI to others — in interviews, several clients volunteered examples where they had actually encouraged friends and family to talk to the CDFI and/or had distributed leaflets for the CDFI in their community.

“In-roads has given me the opportunity to prove I am a responsible person.”

Quote from Robert, In-roads dvd

Eighty-six per cent of clients surveyed indicated that their loan was “exactly what I was looking for”. Client’s comments identified five aspects of the CDFI product as most attractive.

1. Characteristics of the loan; specifically flexibility, with no extra charges and penalties if there is a temporary setback.
2. Customer service. Clients appreciated the CDFI’s personal service and the fact that they were offered a fair go. This was summed up by one respondent as “The staff are compassionate and helpful and make you feel worthwhile, just in a bad spot”.
3. Impact on financial circumstances. Loans assisted people to improve credit rating and get “their lives back on track”.
4. Personal achievements such as the establishment of a business, completing study or car purchase made possible by the loan product were important.
5. The quick and easy processes for establishing and repaying loans were appreciated.

6.3.4. What was the experience of CDFIs in working with investors?

Each of the CDFIs had a unique type of relationship with their investor.

Many Rivers – Westpac

Westpac initially became involved with Many Rivers through a previous pilot, which was able to demonstrate the viability of the Many Rivers model. Westpac commented in interview that without this previous pilot experience, it would have been difficult to present a credible business case for the project as there were too many unknowns/ areas of risk. This experience allowed the project to demonstrate success in loan repayments and arrears management.

Current business partners highlighted the main reasons why Westpac became involved with Many Rivers. This included:

- the synergy between the business goals of the organisation and Many Rivers’ mission;
- the strong relationships built with clients, communities and the investors; and
- the professionalism of Many Rivers, particularly in the area of reporting on outcomes and achievements with clients.

In contrast to the other pilot organisations, Many Rivers acts as an agent of Westpac rather than being licensed to lend directly. In this way, it is unique within the CDFIs as not being limited to a specific capital pool. It is unclear at this stage whether such arrangements would be replicable, and it means that Many Rivers does not earn interest on the funds loaned to clients (unlike Fair Loans and Fair Finance) although Westpac does make a donation to Many Rivers equivalent to the interest earned.

Many Rivers was the only CDFI to employ a business development manager, and achieved unrestricted (that is not designated for a particular project) funding of \$198,000 in 2010-11 and \$100,000 YTD in 2011-12.⁶⁰

Fair Loans/ Fair Finance – NAB

⁶⁰ Report on Many Rivers performance 19 March 2012.

NAB reported that it has an ongoing interest in the wider financial inclusion agenda, and it is keen to explore potential of CDFIs to create alternatives for underserved consumers and pathways to the mainstream. NAB has provided extensive financial and in-kind support to other microfinance projects, notably NILS and StepUP.

For Fair Loans and Fair Finance, NAB support assisted with funds to lend and recycle once loans were repaid. NAB undertook regular audits to ensure agreed procedures were being followed.

In roads – Bendigo Bank

Bendigo's relationship with In-roads is somewhat different than the other pilot-investor relationships, given the status of CSB as a Bendigo franchise. As a result of this status, Bendigo sees itself as having a mandate to focus on the community sector and financial inclusion.

This was not, however, without its problems. Ensuring In-roads processes were compliant with Bendigo's requirements caused some delays during the pilot and should the program continue there may be opportunities to streamline and improve some aspects of the process with advice from Partner organisations.

Community Credit Foundation – Fitzroy & Carlton Community Credit Co-operative

The CCF explored the possibility of lending under the Co-op's licence while it sought financial contributions towards both operating costs and lending capital from credit unions and other supporters. They did not have a capital pool and it appears unlikely that this venture will proceed.

Social Investment

Foresters and CSB are in the process of establishing vehicles to facilitate social investment by other organisations and thereby create a larger loan portfolio.

6.4. Effort – how hard did we try?

6.4.1. What factors influenced any variations in results between pilot organisations?

International experience suggests that it will take some time for a CDFI sector to become established in Australia. CDFIs in the UK, for example, took 16 years to grow from just three CDFIs in 1984 to 27 in 2000; numbers then grew fast with a peak at 80 organisations in 2007. This was stimulated by the UK Government's Phoenix Fund (£42 million revenue and capital grants to assist CDFIs to grow and innovate in the period 2000-2008); and Growth Fund (£100 million financial inclusion strategy providing revenue funding and capital for on-lending to individuals by CDFIs and credit unions in the period 2006-11) (GHK 2010). Numbers of CDFIs now stand at 66 (CDFA 2010).

It is also important to note, as with any innovation, there is a significant amount of time required for the design and set up phase of the initiative. Some slippage in projected timeframes has already become evident across the CDFIs involved in the pilot, with one organisation yet to make a loan. It would appear that the pilot program has been disadvantaged by an unrealistic expectation of pace of establishment from the outset.

Notwithstanding these constraints, the pilot presents an opportunity for the features of the different models of CDFI to be explored. Some of the main dimensions of difference identified include:

- the age of the model/organisation;

- reach national/local models; and
- social and financial aims.

Each of these distinguishing features is discussed below.

The age of the model/organisation

It is clear that attaching a CDFI pilot to an existing organisation which is already offering the same/ similar products and services is a major advantage in start up. Many Rivers and Fair Loans were able to be active lenders from the commencement of the pilot and have achieved anticipated targets.

Those providers who were starting from scratch appear to have been overly optimistic about the number of clients they would be able to attract in the pilot period. These providers are unlikely to achieve the lending targets anticipated because of the time taken to address set-up issues. Fair Finance and In-roads required significant work to become legal entities, recruit staff, design and gain approval for systems and procedures and secure their lending capital. CCF is in the final stages of establishment and has made no loans yet.

One impact to note is that no actual “like for like” comparison will be possible between CDFIs based purely on numbers of loans achieved at the end of the pilot.

Reach: national/local models

One of the challenges recognised internationally which is faced by financial institutions such as CDFIs and credit unions is achieving scale whilst retaining a local, recognised and trusted face (Jones & Ellison 2011).

Many Rivers is a multi-site initiative, operating in diverse locations in both NSW and WA. However, at the grassroots it is very local, with field officers recruited and working in their local communities. This creates a significant fixed-cost base for the initiative, but comes with the benefit of creating the capacity to provide local direct support to individuals and their fledgling businesses. Feedback from funders emphasised the importance of this relationship-based approach and cautioned against rapid growth at the expense of maintaining these strong relationships.

Fair Finance and CCF are both local models, deliberately targeting specific geographic areas of disadvantage using shopfronts. Both have sought to increase their geographic reach through developing alliances with NFPs such as Good Shepherd to identify and develop a range of supports to clients through mutual referrals and outreach activities. Fair Finance is developing outreach bases in neighbourhood centres in South-East Queensland.

In-roads combines a local and central model using a hub and spoke approach, drawing on the networks and expertise of partner agencies to undertake the individual work with clients. This appears to have benefits in terms of scale and reach into disadvantaged communities and is potentially further replicable. However, there are drawbacks emerging in that CSB needs to ensure partners engage actively with marketing In-roads and that they adopt a consistent approach to lending. There are also significant variations within the models adopted by the In-roads partners, and in their results. Stronger results in terms of loan numbers appear to have been achieved by the organisations that appointed dedicated relationship managers for In-roads rather than linking the work to existing teams, however, this has led to a short-term project based approach. The roles are not within establishment or core work and will cease when the funding ceases. Amongst the partners, the O Group is the only organisation with plans in place to continue In-roads via existing

employment adviser posts should CSB continue lending. In two welfare-based agencies, In-roads does not appear to be a good fit with their usual client group, and the very similar criteria for eligibility between In-roads and StepUP loans may have decreased the pool of people for whom an In-roads loan was suitable.

Fair Loans uses a national, web-based model. Their clients are more likely to have wages rather than government benefits as their primary source of income, and automated loan assessment followed by manual screening of bank statements for verification means that clients in complex situations (for example, an incorrect credit history) will have an automatic exclusion. Fair Loans is also seeking to test outreach into a specific local community through a partnership with an NFP and the establishment of a quasi-branch for people who do not have the information technology necessary (computer, fax or scanner, printer, email) to make use of the web-based channel. A third element is testing the targeted use of a Money Mentor dedicated to Indigenous engagement in the branch.

Scale was also a key message from the NAB study which highlighted the costs of making small loans using a (relatively) low cost and efficient internet based model (NAB 2010). In that pilot, the administration cost was over \$300 per loan in a purely financial model. This did not take account of expenditure required, for example, for money mentoring, referral or budget support — activities which are built into the CDFI approach. This means costs per loan will be higher for CDFIs, with even the online model requiring further economies of scale.

Social/financial aims

All of the pilot organisations have social aims. As noted earlier, a challenge for CDFIs is balancing the social purpose of assisting people who are underserved by the mainstream, with maintaining a sustainable business. Some of the key challenges emerging relate to:

- the importance of relationships and one-to-one interaction with clients;
- building capacity in clients via the quality of the work done with them, ideally building confidence and empowering them to solve financial problems in the future; and
- identifying policies to drive decisions in borderline cases. All of the organisations discussed how they balance protecting their balance sheet (and ultimately organisational sustainability) with supporting clients in difficulty. These decisions tend to be made on a case by case basis with the need to avoid client hardship forefront.

The culture of the organisation is significant. It is notable that in the set-up phase, all CDFIs have identified the importance of recruiting staff who not only have the technical skills, for example to assess a loan application against agreed criteria, but who can also appreciate the social mission of the organisation and look for ways to assist people either by referral or recommendation of more suitable products.

One area explored in interviews with some CDFIs and In-roads partners was the notion of incentives for staff with the aim of increasing the number of clients with loans. This was strongly rejected by all interviewees and illustrates an important difference between a commercial provider and CDFI. The key issue is the successful outcome for the client, not the number of products 'sold'.

While financial literacy training sessions were envisaged by most of the pilot organisations initially, this thinking has changed to focus more on the one to one interview process. Interviews with staff working in CDFIs directly with clients reflected the importance of good communication with clients and the critical nature of the time invested in discussing a financial situation and resolving issues. The experience with the CDFI pilots would appear to substantiate the views of Proske (2010) who researched activities to achieve behaviour change in financial matters in low income clients. She comments

One-on-one counselling is most effective —experience in the US, Ireland and UK suggests that individual counselling results in the greatest level of behavioural change as individuals' specific circumstances are considered.

Financial education is most effective when coupled with an appropriate product offering — US and UK experiences strongly suggest that it is essential to couple financial education with an appropriate product (loan or savings program). This increases the attractiveness to clients and leads to better outcomes.

6.5. Effect

6.5.1. What were the outcomes for clients?

Over the course of the pilot, CDFIs have lent a total of \$2,827,628 to 1,175 people. It is early days in terms of assessing results, however, the main outcomes for clients appear to be:

- the achievement of loan purposes; loans have been provided to assist people to buy household items, repair or purchase cars and pay off other credit or defaults;
- the focus on white goods and car repairs reflects key needs of people with low incomes and are consistent with the results of other lending programs such as NILS and StepUP;
- the CDFI loans assist people to pay off debt and create a positive credit history; this is not an option with NILS and Step Up and is a key point of difference in the programs;
- financial stress is common for borrowers, some interviewees and lenders describe people making use of food vouchers, food bank and free meals, or going without meals;
- without the support of the CDFI, clients reported a high reliance previously borrowing from friends and family and alternative forms of lending such as payday lenders. Many had been turned down by mainstream banks in the past;
- two-thirds of follow-up survey respondents reported that the loan had made an impact in reducing their financial stress levels;
- for the face-to-face lenders, a key outcome is providing individuals with a detailed understanding of their financial circumstances achieved through the loan application

process. Examples were given of people discovering they had inaccurate credit records, resolving long-standing issues with creditors and achieving significant financial savings. Many more people have been assisted than eventually take on loans. Through the supported application process they achieve an understanding of their income and expenses. These outcomes are only possible because of the time spent with people and the trust built between CDFI worker and client.

- 144 new businesses have been started or supported to become established;
- for people in disadvantaged areas, support from Many Rivers to identify their personal goals and assistance in creating plans to achieve realistic businesses can be transformative; again time and trust are key ingredients;
- three of the initiatives — Many Rivers, CAIE and KES — work with a majority of Indigenous clients. Feedback suggests that the results being achieved with a target group that typically very challenging to work with are very positive. Indigenous people are over represented as severely; or fully-excluded consumers of financial services compared with the rest of the population, and are more reliant than other groups on fringe non mainstream credit (Connolly et al. 2012).

Case Studies

Mary

Mary is in her 60s and looks after a disabled child. She was facing a lot of problems because her car was not roadworthy and without it, getting around with her daughter was impossible. She tried to get a loan from her bank but they were not interested because she is on a pension. She approached another bank and they wouldn't accept her because she had no credit rating — she has not borrowed any money for many years and always pays her bills up front. A friend told her about In-roads. She is very happy with her \$3,000 loan. It costs her \$66.20 per fortnight and she likes paying by direct debit so that everything is on track and organised.

Survey interview 2

Tina

Tina is a divorced mother. She has four kids and is desperate because her ex-husband wants to take the car. Without a car she would have no way to get the kids to school. Tina is very independent — in the past she has had to borrow to cover the costs of Christmas and school fees from friends and family and repaid them as soon as she had the money or worked by cleaning their house to pay them back. She has had to go to the Salvos for help with food hampers and once went to payday lender, she says she hated that, she felt degraded.

Tina talked to a bank but they were unable to offer credit because she only works part-time. Through In-roads she was able to borrow \$4,000 to buy a car. She has already paid half of her debt.

Survey interview 6

6.5.2. How many people met their loan obligations?

Given the concerns of mainstream lenders about risks of default in providing credit to people who become CDFI clients, arrears are an important indicator.

None of the CDFIs report significant concerns with arrears, although it should be noted that for two of the lenders there was less than nine months of lending history, and most of their loans were made in the final three months of the pilot.

For In-roads the role of the relationship managers is as a direct link with clients and this has assisted in the management of any queries.

While Many Rivers had the highest number as a proportion of total loans, their experience suggests that clients remaining in contact with the organisation will repay their loans eventually.

In comparison, NILS reports arrears of under 5 per cent in 2011⁶¹ and the NAB small loans pilot loan defaults 4.16 per cent (NAB 2010).

Table 38: Arrears

	Many Rivers	Fair Finance	In-roads	Fair Loans
Clients in arrears	32 (26%)	None	3 (1.9%)	55 (6.6%)

6.5.3. What were the outcomes for CDFIs?

The pilot has enabled four organisations to establish or expand their work as financial intermediaries offering personal loans to people who would otherwise be unable to access credit.

Many Rivers

The CDFI pilot funding has assisted Many Rivers to grow from three to nine regional offices. Many Rivers expanded its activities and staff team over 2011–2012 and established new offices in Moree and Blacktown, NSW, as well as Perth. A new Queensland office opened recently in Cairns and a Condobolin office will open in July 2012 in NSW.

In 2011/2012 Many Rivers Microfinance reviewed its positioning as an organisation and plans to rebrand as 'Many Rivers'. This change reflects their role in community development work. Rather than emphasising the provision of microfinance, arranging loans is just one element of the supports offered.

Fair Finance

Fair Finance was a new initiative for Foresters. The establishment of the CDFI involved securing office premises and recruiting a new staff team as well as setting up all of the loans systems and processes. A new brand identity was created supported by marketing materials and a website. As a pilot, FFA took the opportunity to experiment with different methods of outreach to clients, including working with community organisations and in shopping centres. The conversion rate (enquiries converted to loans drawn) is 8.5 percent, so it is important to maintain a strong pipeline of interest in the CDFI.

⁶¹ <<http://www.goodshepherdmicrofinance.org.au/services/no-interest-loan-scheme-nils>> accessed 20 June 2012.

Foresters now offers a range of community finance and social investment products. Fair Finance was accredited early in 2012 to offer NLS loans, and has also developed a small business loans product and a no interest loans product for individual artists. Foresters was selected by the Australian Government to establish and manage two funds to support social enterprises under the Social Enterprise Development and Investment Fund (SEDIF). Foresters was awarded \$6 million, with initial leverage from investment partner Christian Super creating a \$12 million fund.

In-Roads

In-Roads set itself an ambitious agenda in creating a network across Australia of organisations offering a new loan product, with a new brand identity, materials and website. It was able to establish a presence with its not-for-profit partners in six states and the Northern Territory, and has the potential to achieve scale. The initiative took longer than anticipated to start lending, primarily because of questions of detail in loans documentation required by Bendigo Bank. There was also a learning curve reported by Relationship Managers who needed to be trained in the loans process and how to assist loan candidates to apply.

Results varied between partners, and should CSB decide to continue with the In-Roads product it will be able to apply learnings from the most successful.

Fair Loans

Fair Loans was able to build on the experience of running Money Fast and had systems in place to offer web based lending from day one of the pilot. The Money Mentor was a key addition to their work as a CDFI, with positive feedback about the support offered.

As a new social enterprise, they moved into work in Indigenous communities through CDFI.AB and Indigenous community engagement. They also provided grants to assist Indigenous education projects in Werrington Public School.

CDFI sector

Over the course of the pilot, CDFIs worked together in responding to government initiatives and met on several occasions to share experience and learning. They also made a contribution to the sector as agencies working on financial inclusion as members of AFIN. Feedback suggests it will be important in the future to ensure that there are opportunities to maintain collaboration and share learning.

6.5.4. Is there a community level impact from CDFI?

The short duration and limited scale of the pilot provides no opportunity to assess community level impacts from the work of CDFIs.

Some of the potential benefits of CDFIs that could be examined in any future study include:

- impact on local economies through supporting enterprise and the creation of jobs;
- financial resilience so that individuals and communities are better able to respond to problems as they emerge;
- early intervention to assist people before they are in crisis;
- decrease in the need for individual emergency relief resources;
- individuals who understand their finances and are confident making financial decisions, and pass those skills to their children.

The economic and social impacts on communities of high numbers of fringe lenders could also be investigated.

6.5.5. Is the model financially sustainable?

It was assumed at the start of the pilot that philanthropic investment could be attracted to support CDFIs, and that Deductible Gift Recipient (DGR) status would assist in this effort. A small number of Australian NFPs (25,292 in 2008), are eligible to apply for (DGR) status from the Australian Tax Office. Donations to DGRs entitle donors to claim tax deductions and allow organisations to attract funds from grant makers and philanthropic bodies such as Foundations.⁶²

Many Rivers is the only CDFI to have attracted widespread philanthropic and business support.

Fair Loans was not successful in their application for DGR status, which may reflect the balance they present between social and financial aims and activities. In a note of caution, Burkett (2010) highlights the risk which dependence on grants and gift capital poses to the sustainability of social enterprises, noting that where core operating costs cannot be covered without grant capital then the enterprise will not be viable.

The costs associated with assessing an application, setting up a client account and managing that account is the same regardless of the loan amount and the fees or interest earned. This has an impact on the sustainability of the lending organisation. Reducing the number of small loans may be one option to improve cost efficiencies (DWP 2012), however this may conflict with the social mission of CDFIs and further exclude people who are unable to service a larger loan, or force people to borrow more than they actually need. Another option is for CDFIs to set up loans for longer terms, thereby earning more interest as the principal outstanding is reduced at a slower rate. Such a strategy may be beneficial for some clients but detrimental to others and raises an issue of fairness, discussed in section 7.2 following. It also ties up the capital available to lend for a longer period and so could increase the funding pool required by the CDFI or limit the number of borrowers it can support.

6.5.6. Compliance with Legislation

As credit providers, CDFIs are required to comply with the National Consumer Credit Protection Act 2009 (NCCPA), the National Credit Code (Schedule 1 of the NCCPA) and the Australian Securities and Investments Commission Act 2001.

The NCCPA commenced in 2010 and established, a single, standard, national law for the regulation of consumer credit which provides protection for all consumers seeking to access consumer credit. This protection is particularly important to those who are at risk of financial exclusion and CDFIs have a responsibility to ensure that they are compliant with this legislation.

After the commencement of the pilot, ASIC was asked to provide general information and deliver a presentation to FaHCSIA staff and participating CDFIs on the NCCPA and the compliance obligations of the CDFIs. During the presentation, ASIC provided information about the nature of credit activities, the requirement to be licensed, responsible lending and disclosure obligations and the requirement for CDFIs to maintain membership of an external dispute resolution scheme.

There were some compliance issues experienced during the CDFI pilot. Fair Loans provided inaccurate contract documentation and overcharged interest to clients. Fair Loans remedied this

⁶² <<http://www.givewell.com.au/statistics.asp>> accessed 20/11/11.

breach, agreed to pay two infringement notices and agreed to engage a compliance consultant. After the pilot period, Foresters advised that ASIC had concerns over their website advertising, which they remedied immediately upon notification. Foresters agreed to pay an infringement notice. These issues highlight the complexity of the regulatory environment for emerging CDFIs and the need for ongoing monitoring of CDFIs and education on the importance of compliance.

7. Discussion

Across the four active CDFIs there was a total loan book value of \$2,827,628 at the end of the pilot. This represented:

- Micro credit of \$668,545 supporting 144 new businesses by Many Rivers. A total of 367 people accessed business planning support, with over 200 people in a pipeline to start businesses; and
- 1,053 personal loans, totalling over \$2,159,000.

However, only two CDFIs met their targets for client numbers and loans established for the pilot. Two were able to achieve less than half the numbers anticipated and one did not make any loans. The scale of the pilot has thus limited what can be learned, especially given the wide variety in the models.

7.1. How effective were the CDFIs in increasing the ability of disadvantaged individuals to gain access to appropriate credit?

All of the CDFIs have assisted disadvantaged people at risk of financial exclusion. The survey of borrowers indicated over half of the respondents had the experience of having previously applied for a loan and being rejected. When they had been able to obtain previous finance, Many Rivers, In-roads and Fair Finance clients indicated the most common source of previous loans had been Centrelink advance payments. This may be problematic given the limitations of Advances. Approximately one-third of previous borrowers had sourced loans from either payday lenders or pawn brokers. Another 22 per cent had borrowed from a finance company. While responses from Fair Loans clients also indicated a high proportion of Centrelink advances, there were also higher levels of borrowing from finance companies amongst this group. Notwithstanding the small numbers, this feedback suggests CDFIs are assisting some people to avoid more expensive payday loans. In interviews with WestWood Spice, several clients spoke about their determination not to return to 'Cashies' and other forms of short term lending.

Almost 30 per cent of borrowers across the four CDFIs identified as Aboriginal or Torres Strait Islander. This is an important contribution of the pilot as Indigenous people are over-represented as users of non-mainstream credit and may be additionally vulnerable to payday lending (Connolly et al. 2012). The proportion of Indigenous people is highest for In-roads (64 per cent) and lowest for Fair Finance (8 per cent). The picture which emerged from survey respondents is one of a history of considerable financial hardship with a high reliance on alternative forms of lending such as payday lenders. People also mentioned making use of food vouchers, food bank and free meals from religious groups.

A third more women than men have taken out personal loans, however more men than women have enterprise support through Many Rivers. Over a third of Fair Finance and In-roads' clients have a disability.

Loans have been provided to assist people to buy household items, repair or purchase cars and pay off other credit or defaults. The focus on white goods and car repairs reflects key needs of people with low incomes. This is consistent with the results of other lending programs such as NILS and Step Up. A particular strength of the CDFI model is that personal loans could also be used to assist people

to pay off debt and create a positive credit history. This is not an option with NILS and Step Up and is a key point of difference in the programs. Through credit checks, CDFIs are also able to assist people who have defaults on their record of which they are unaware, the defaults may even be there in error, preventing access to mainstream bank options.

Feedback from clients indicates the features of the CDFIs they liked most were:

- characteristics of the loan — flexibility, payment terms, no penalties if there are temporary setbacks;
- customer service — described as personal, understanding and the staff easy to talk to;
- Impact on financial circumstances — “helping to get my life on track”, “fairness”, “avoiding financial disaster” (the words of clients);
- benefits due to loan purpose — such as being able to use a car, study or start a business; and
- method of securing and repaying the loan — clients found the process straightforward and direct debits easy to manage.

One issue identified in the evaluation was that the eligibility criteria of some of the CDFIs were restrictive. For example, using eligibility criteria such as “income below \$50,000 per year” appears to have been unnecessarily limiting. More flexibility around eligibility could increase assistance to greater numbers of people who are currently financially excluded.

Client documentation and administration systems could benefit from significant simplification. This will assist clients in their application and enable efficient loan processing while complying with all regulatory requirements. The use of transparent documentation which explains interest payable and the weekly/fortnightly/total commitment is a major benefit to clients in assessing affordability of loan products.

7.2. Is the demand for appropriate financial products and services best met by CDFIs?

People on low incomes and those with poor credit history currently have very limited options if they require additional funds (Banks et al 2012). It is significant that a CDFI loan is not “charity” and offers people the opportunity to be self-reliant and transition to the mainstream.

CDFIs act in the interests of clients, recommending alternatives to loans where more appropriate. This is very different from the commercial situation where the key driver is the profit generated for the organisation.

Pilot organisations were all able to supply examples of where services such as budget advice or debt renegotiation had been supplied to borrowers, and for all of the organisations except Fair Loans such services were also accessed by people who did not have loans.

The CDFI relationship-based models adopted by Many Rivers, Fair Finance and In-roads partners worked one-on-one with very disadvantaged clients and helped them to establish businesses or resolve financial problems. “It is not about loans” was emphasised by providers, however access to a financial product, supported by a relationship-based approach can encourage financial participation and behaviour change (Proske 2010). There is early evidence that the approach is gaining traction, most notably in Aboriginal communities when introduced by trusted workers, across three different pilot models.

Web based products have the potential to achieve scale and to reach much larger numbers of people who may be unable to access a face-to-face service, but they are very different in impact. Fair Loans was the only organisation to have a majority of clients with wages rather than government payments as their primary source of income. The Fair Loans model was good at solving short-term funding problems but phone and email contact with the money mentor may not be as effective in encouraging longer-term behaviour change. Many clients require face-to-face work which a web-based service cannot replace. They may provide a very useful adjunct to face-to-face services if collaborative models can be developed. WWS understands Fair Loans was beginning to explore such relationships.

It is important to emphasise that a CDFI just one option to address the issue of financial exclusion and is not able to meet demand for very small loans (people who want \$50) for a couple of weeks or where income is inadequate for day to day expenses.

It is important to build scale so that economies can be achieved by individual lenders and so that there is wider awareness of what a CDFI does. The UK experience suggests this will take time. Nevertheless CDFIs can play a key role in addressing financial exclusion as part of a multi-faceted approach including subsidised no and low interest products and licensed short-term, high-interest options.

Client's experience

"I tried everywhere to get a loan to repair my car. People talk and they said you should try this new place. I went down and had a yarn and filled out everything. Then they did a credit check. It said I owed \$700 to a phone company — but that was wrong that was all paid 6 or 7 years ago and I could prove it. I gave In-roads permission to talk to them and they sorted it all out and now my car is repaired."

Survey respondent 13

Funding and sustainability

Should the CDFIs receive further government subsidy? The context is important given the increasing problem of financial exclusion and the rise of payday lending.

Recent studies indicate that the number of people financially excluded has grown and is likely to continue to grow (QCOSS 2011; WACOSS 2011; Connolly, Georgouras M & Hems 2012). While a CDFI loan is not a remedy for inadequate income, CDFIs can play an important role in intervening to stop debt accumulating or defaults occurring and prevent the worsening of a bad situation for people on the fringe. The flexibility demonstrated by CDFIs is important, for example allowing early repayment or extension of the term of the loan without additional charges.

Government is acting to curtail payday lending but the reality is that there are few alternatives in place for people who are excluded by mainstream banks (or exclude themselves). Fair and accessible alternatives are required. In considering the definition of fair, both the (effective) interest rate and term need to be considered.

From the borrower's perspective, while the total amount paid over a short-term will be lower, this may be more difficult to repay on a week-by-week basis compared with a lower weekly amount which adds to a higher total repayment over a longer term. Clients interviewed knew the exact amount of their regular repayments and the term of their loan. This is important for affordability.

Among the pilot organisations, Fair Finance developed a tool to help borrowers understand this relationship and to guide them in selecting a manageable repayment level and timescale. This is an essential tool for all CDFIs as the APR is not understood by clients.

From the loan provider's perspective, if an interest rate is too low or a term is too short, a CDFI may not be able to generate sufficient income to continue operating. The appropriate rate must balance this pressure with the need to take account of the low income of CDFI clients and the impact of borrowing on their overall ability to have a reasonable standard of living (QCOSS 2011). It is here that the role of government needs to be considered.

Early feedback from clients suggests two factors are most important to clients:

- *Timeliness*: The availability of the loan when they need it, for example to solve a problem like a car needing repair.
- *Service Quality*: The quality of the personal service they receive from the CDFI and the level of trust which is established. This might mean identifying and solving a problem such as fixing an incorrect credit history or providing sufficient funds to both pay debt and repair a car. Every person interviewed knew the name (unprompted) of the CDFI staff member who assisted them with their loan.

Higher interest rates have been justified in theory on the basis that clients carry a higher risk, however, the experience in the pilot to date has been one of low arrears and defaults. This suggests that many clients are not necessarily higher risk but rather are more costly to service because of the individualised support required.

The pilot uncovered an uneasiness amongst financial counsellors with the recommendation of an interest-bearing loan as part of a solution to a person's poor financial situation. It is also interesting to note that the recent conference of financial counsellors included a session directly targeting this reticence.⁶³ In the case of one provider (St Luke's), this was overcome by a clear separation of personnel to avoid any conflict of interest. A 'welfare' approach conflicts with a 'hand up not handout' approach — the CDFI emphasis is on assisting people to find solutions they can afford and prevent problems occurring.

Web-based lending is somewhat different. The pilot experience is that only a small proportion of borrowers used the Money Mentor service until they were required to. The cost of delivery is less than in the other models. Notwithstanding this, the web-based model will still require a significant increase in scale to reduce the cost per loan to a level which is self-sustaining in the longer term. While Fair Loans clients are more likely to be in employment than other CDFIs' clients, they are nevertheless on low incomes and report being unsuccessful applying to the mainstream banks for credit.

It may be helpful to consider the CDFI process as having two elements:

- the loan; and
- the individual support.

A sustainable target in the short-term might be CDFIs working towards blended income with financial products that cover intrinsic costs of the financial transaction (the cost of managing the actual loan) whilst requiring subsidy (government and philanthropic) for the costs of assessing and

⁶³ Dr Therese Wilson, personal communication.

supporting clients. This is a division made for modelling purposes illustrated below. The two elements are intrinsically linked; the financial product provides the incentive for clients to contact the CDFI and access support, such people may otherwise might worsen their financial situation (through for example, the use of payday lenders) or not seek advice. Good support means good financial returns, low arrears and positive word of mouth marketing. Good support also means loans are made prudently; it is essential to protect the capital so that it is able to be re-lent; and to ensure positive client outcomes. Loans are not made which would violate responsible lending.

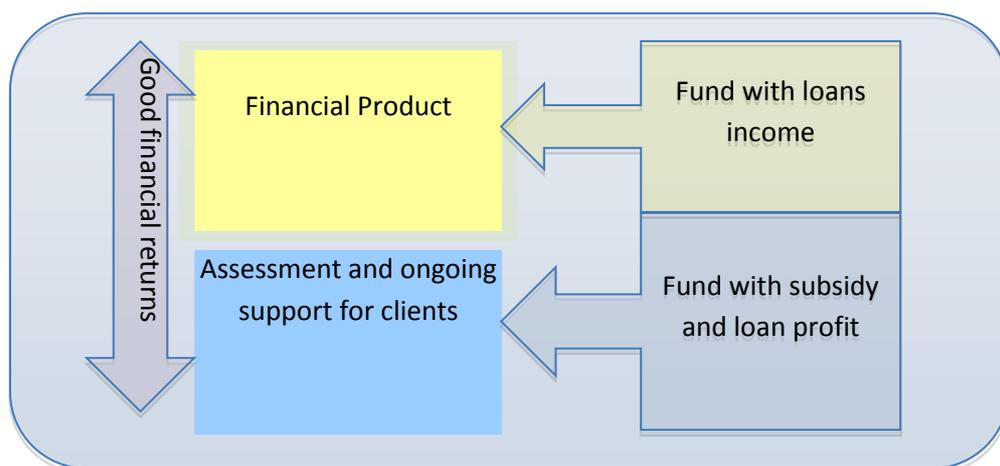


Figure 3: Blended income

Impact

The CDFI sector is characterised by an explicit social mission. This is best illustrated by the Foresters' founding principles. These principles position CDFIs as addressing the financial exclusion of individuals, social enterprises/businesses, and community sector organisations. What is distinctive is the clear social purpose and aim to deliver wealth creation and asset building into communities that are most disadvantaged or underserved. The role of the CDFI is to channel investment and support people to 'access the capital needed to build their assets as a pathway out of poverty' (Foresters 2009). It is important to consider the role of the CDFI in both creating opportunities to access capital and building the skills, knowledge and attitudes to apply the capital. The role of individualised support in the Australian context would appear to be key.

As noted earlier, the role of the personal lending CDFIs is complementary to the work of other agencies in financial counselling and emergency supports. At scale they might act as a preventative measure, assisting people before problems. Individual loans via web based might be helpful in preventing people using payday lenders but without individualised support services they may only be a temporary solution for clients in financial hardship.

Evidence that a CDFI is having a positive social benefit is obviously important and the results of such measurement will be of interest to supporters and funders. However, the measurement of social impact is a new science (CCS 2011) and there are a number of challenges. These include:

- *Attribution*: particularly where community as well as individual benefits are sought, change is more likely to be the result of combinations of interventions rather than single initiatives.

- *Timing*: complex problems are rarely simple to resolve and may take several years, with slow progress barely discernible. Many Rivers for example has stated publicly that in order to have an impact it is committed to working with communities “for the long haul”.
- *Some areas are hard to quantify and measure*: benefits are tangible (less debt, more assets, higher employment) but also attitudinal. Studies in the UK, NZ and Australia have found that enabling people to have a greater sense of control over their own lives was one of the most significant benefits of working on financial issues (NZ Government 2009; GHK 2010; Russell, Bailey et al. 2011). Other benefits may include increased social capital; with CDFI microenterprise borrowers reporting, for example, that they now act as positive role models in their communities and can help other people (GHK 2010; Many Rivers dvd 2011). Again this is an important but difficult area to quantify and measure.

7.3. The mechanisms and barriers CDFIs face in gaining access to capital

An original premise that operational costs will eventually be covered by the income generated from a capital pool plus interest on loans appears to be unsubstantiated for several reasons:

- In an Australian context, it is hard to imagine a CDFI reaching the scale required for viability. The size of population in a city such as Brisbane is not comparable with London or Chicago.
- Overseas experience shows that personal lending CDFIs are impossible to operate without subsidy except in the cases of the largest organisations.
- A web-based product may achieve scale with sufficient promotion, an adequate interest rate and a strong focus on the lowest possible administration costs. Such CDFIs could play an important role in providing safe and ethical loans to people on low incomes but are unlikely to reach the most complex/challenging clients and will not provide any service to people who do not meet their eligibility criteria.
- Overseas experience suggests efficiencies may be achieved if CDFIs develop other financial products such as NFP and enterprise lending or insurance, however the Australian markets for these other products are still likely to be fairly small.
- The costs of operations outside capital cities in Australia are prohibitive. Without significant ongoing subsidy, working in rural and remote areas of Australia is not sustainable.
- Although it is early days and the scope of this evaluation is limited, there is no evidence that investors would be interested in contributing to a capital pool as an impact investment. The current arrangements provide funds to recycle at no cost to the CDFI or lending from the supporting bank’s balance sheet. With the exception of Fair Loans, the capital has been adequate to meet client loan requirements. The issue is one of meeting substantial operating costs going forward.

There is evidence that the Many Rivers model, with a focus on individual enterprise and client support is more attractive to funders, and they have been successful in securing longer term commitments from their backers.

7.4. Challenges

Challenges faced by the CDFIs that may need to be considered in any future models include:

Costs of service delivery

CDFIs consider the work to establish people's circumstances and commitment to repaying the loan is essential to the loan process. CDFIs can also provide assistance and referral where loans are not suitable and builds skills so that the client understands their finances. Numerous examples were provided both by CDFIs and clients of such assistance, including negotiating with creditors, restructuring debt and finding more cost effective solutions to financial problems. It would be possible to argue that this intensive work duplicates the role of financial counsellors, however a key difference is that many CDFI clients would not consider going to a financial counsellor or welfare organisation for aid, but accept support in the context of a loan application process. A study by the Wesley Mission (2010) including a survey of 621 people found that only one in twenty people would seek help from a financial counsellor if they had financial stress. Proske (2010) found that there were better behaviour change outcomes where financial skills development was linked to access to a financial product. Undertaking advice work can also be beneficial to the lending organisation; the CDFI (2009) reported that CDFIs providing financial advice had an average default rate 3 per cent lower than those providing just finance. UK studies have also identified as an issue the considerable time and money spent by CDFI staff on clients who do not end up receiving a loan (Dayson 2008).

Recommendations to increase CDFI sustainability have included minimising the time spent with applicants (Dayson 2008; GHK 2010; DWP 2012) however this strategy may be counterproductive if the long-term goal is client financial inclusion. The pilot organisations are still developing an understanding of the intensity of face-to-face work their staff are able to manage, but in the Australian context factors such as the long distances travelled by some people need also to be taken into account.

Other learning from the UK relates to seeking cost efficiencies in administrative practices. Some of the CDFIs used manual recording keeping during the pilot. There will be a need to streamline this if numbers of clients grow.

Creating demand for products

As a relatively new service, there is low community awareness of the existence of fair and affordable financial alternatives for small loan amounts. There may be some benefits to be seen from the work undertaken by CDFIs in 2011-12 in creating DVDs and sharing case histories with the media. There was particular feedback from providers that accessing 'the working poor' presented some challenges to those used to marketing through welfare-based channels. Any such promotion would need to focus on brand and reputation to avoid any risk that as a non-mainstream finance option they became confused in public perception with payday lenders. An inherent challenge in the CDFI personal lending model is the constant need to find new customers. The 'best' customer for a CDFI is one who stabilises their financial situation and credit history and is able to access the mainstream. Unlike credit unions, CDFIs are not long term financial providers offering transaction and other services, but try and offer pathways to financial inclusion. The maps of financial exclusion developed by Connolly et al (2012) could be used to inform any future investment to identify areas of greatest need.

Client outcomes

Credit is not a solution for people with income perennially inadequate to meet basic expenses (rent, utilities, food). These people are particularly vulnerable to the impact of large bills such as those associated with health issues, start of school year, Christmas. The number of people in this situation is growing (QCOSS 2011; WACOSS 2011). Borrowing can become an ongoing pattern, and behaviour driven costs (over limit fees, rejected direct debits and penalties for late payments) can significantly increase the cost of credit. CDFIs must stay focused on lending only where this will improve the overall outcomes for the borrower and develop appropriate linkages to other alternatives such as NILS.

Advocacy on behalf of the CDFI client group who experience a wide range of financial pressures is needed. With the increasing cost of utilities for example, there are likely to be more defaults on bills occurring. CDFIs could play a role in preventing defaults, and assisting people to understand and access hardship provisions. CDFIs could also play a key advocacy role for policy change in partnership with other organisations working to achieve financial inclusion.

Clients are judged on their past problems and not their present circumstances. Their treatment is also a by-product of the drive towards greater automation and computerised decision-making, which masks the nuances that help to explain previous financial problems. With so many recovering from the biggest bout of over-lending in history, and growing unemployment fuelling debt problems, rehabilitating damaged credit records, even with good repayments, will not happen. We're going to need the human touch and smarter use of data, or for many the credit crunch will continue for years to come.

Faisal Rahman, *Guardian*, 22 March 2011⁶⁴.

⁶⁴ <<http://www.guardian.co.uk/society/2011/mar/22/credit-debt-unemployment-human-touch>> accessed 22 June 2012.

7.5. Recommendations

The range of models of the pilot has provided an opportunity to make some initial observations and recommendations about the potential of CDFI in Australia.

- Extend the pilot for a further three years. This would allow time to conduct a more thorough analysis of the longitudinal impacts of CDFIs on financial exclusion. It would also facilitate the development of a CDFI sector in Australia. The problems faced by CDFI clients are complex and warrant a cross departmental approach by government to allow a range of measures and impacts to be explored and funded.
- Broaden the scope of the pilot to include lending to social enterprises and not-for-profit organisations. This would increase the social impacts of the CDFIs and provide additional revenue for the CDFIs from the financial products developed.
- Develop tools to review the social impacts of CDFIs at both an individual and community level. This could utilise work being undertaken on social impact measurement by Access Economics and Net Balance in Australia, the Community Development Finance Association (CDFA) in the UK and Opportunity Finance Network in the US.
- Establish a peak body to represent and advocate on behalf of the CDFI sector in Australia. This could facilitate a process of certification of CDFIs, such as the development of an accreditation “kite mark” to identify ethical non-mainstream lenders.
- Explore the establishment of a CDFI fund that provides ongoing financial support to CDFIs.
- Ensure financial exclusion remains the focal point of any future investment in the sector. This can be achieved by ensuring that loan criteria do not exclude people who could benefit, in particular the working poor.
- Promote CDFI activities widely across Australia, specifically working to ensure that CDFIs are easily identifiable by consumers and distinguished from both payday lenders and financial literacy or consumer advocacy and support services.
- FaHCSIA and the CDFIs continue to monitor compliance with the *National Consumer Credit Protection Act 2009*. This includes working with the Australian Securities and Investments Commission (ASIC) to encourage CDFIs to improve utilisation of ASIC’s resources and to encourage CDFIs to facilitate identification of non-compliance with credit legislation at an early stage.

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