

Big Local social investment guide to microfinance



Welcome to the Big Local social investment guide to microfinance!

This is one of four publications that provide more information on topics that we introduced in the Big Local guide to social investment. We encourage you to read the general social investment guide before tackling these more detailed versions.

There are four main types of social investment that Big Local areas can consider. These are:

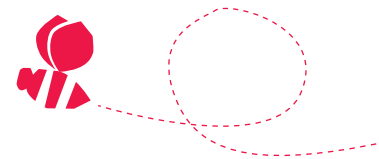
- personal lending
- microfinance lending
- small business lending
- civil society lending.

This guide focuses on microfinance lending. It looks at:

- What is microfinance (using social investment)?
- Why is microfinance part of Big Local?
- What are the risks of microfinance?
- How does microfinance lending work and who administers the loans?
- Next steps.

MORE INFO

You can download the Big Local guide to social investment as well as the four supplementary guides at:
www.localtrust.org.uk/biglocal/resources



What is microfinance (using social investment)?

A social investment is a loan or other financial investment that aims to make a positive economic, social or environmental impact in a community, as well as earning income. Within social investment, microfinance means making small loans to individuals to help them start or grow their own business, when they cannot borrow money from traditional banks. If someone can get a loan from a high street bank, they should not be given a microfinance loan supported by Big Local money.

The average microfinance loan is around £2,500 borrowed for three years, with an average interest rate of 12.3 per cent annual percentage rate (APR). Typical customers

include gardeners, handymen, window-cleaners, hairdressers, driving instructors, small shops and cafés. They may want to borrow money for equipment or vehicles or to help expand or position their business to become more successful.

Using social investment to support microfinance can help to make your area a better place to live. It can also improve life for the borrowers and their communities. For example, to offer loans to local people to start or grow their own businesses. Or you might use social investment to support community finance organisations (see further in this guide for an explanation of what they are).



Why is microfinance part of Big Local?

Microfinance, using social investment, is an important option for Big Local areas to consider, if it can help you tackle particular problems and achieve your community vision. Some of the problems that microfinance can help to address include:

- unemployment, especially among people who are finding it particularly hard to find jobs (including young people, older people, people from black and minority ethnic groups, parents with young children and people with disabilities)
- keeping and circulating money within the local economy
- unused shops, offices and social facilities in your area
- lack of local community services provided for and by local people
- lack of self-esteem among people who are not working, especially in terms of managing and making money.

Microfinance helps local people to start and run their own businesses, creates employment and provides services. It can bring unused shops and other facilities back into use. It helps people to act as positive community role models and improves their confidence. It has been shown to improve not just financial literacy, but also health and mental well-being.

For example, you might decide to work with a community development finance institution (CDFI) or a credit union to offer loans to help young unemployed people start a business, to fund a local business person to fit out and trade from an empty shop unit or to buy a second van so that an experienced tradesman can offer a job to a local person.

Microfinance can offer other benefits to your local area and your local partnership:

1 Impact.

Social investments can have a positive impact because the loans are designed to create economic, social and environmental benefits for your area.

2 Make your money go further.

Each time a social investment loan is successfully repaid, the money can be used to make another social investment. Over time, this means that you may be able to do more with your money and make a bigger impact. You may also earn interest on the loans.

3 Empowering and strengthening communities.

Understanding and managing social investments are very valuable skills. Many people in local areas have never had the opportunity to learn them. By identifying local needs and taking action through social investment decisions, your area can make positive changes to strengthen the community.



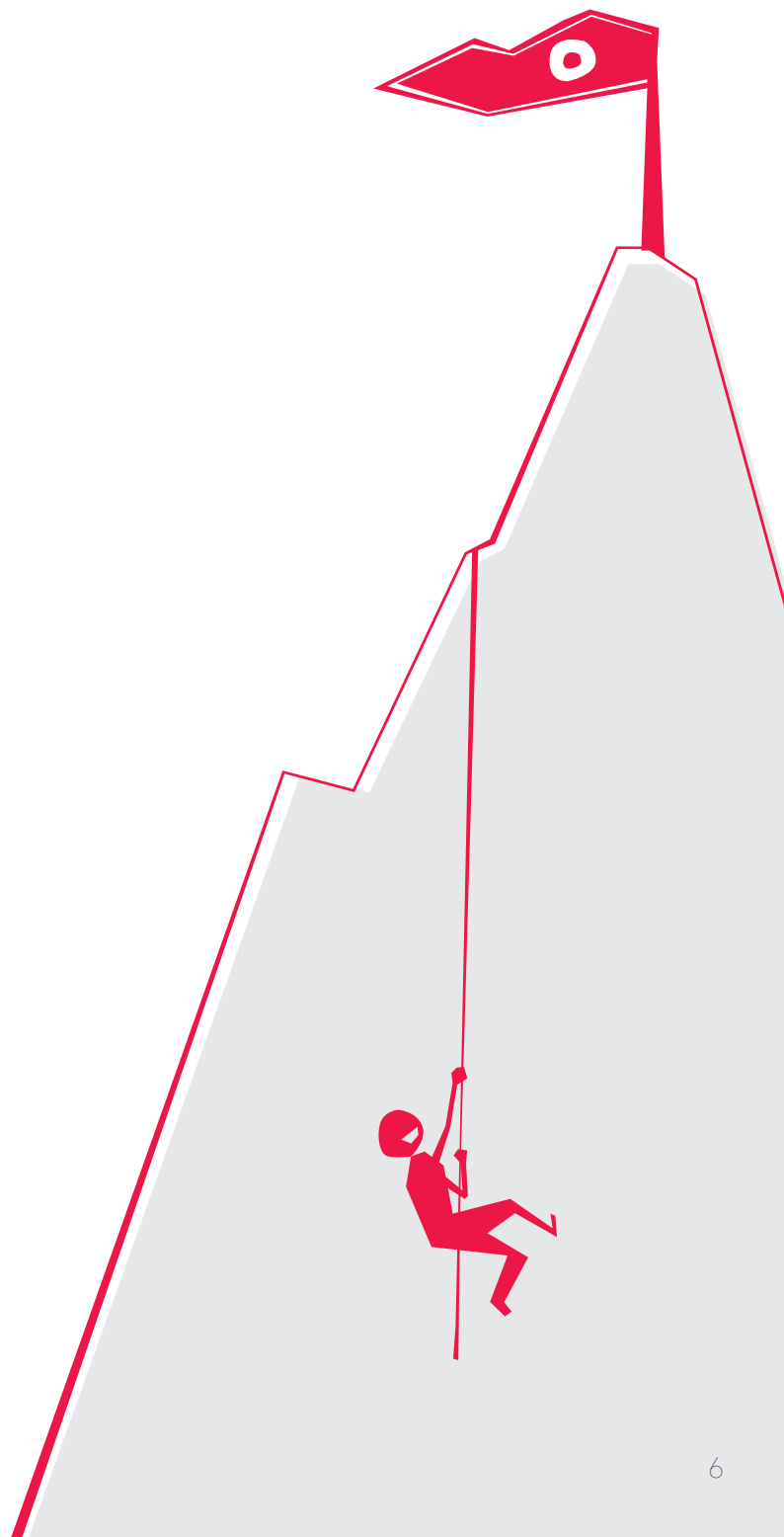
What are the risks?

Sometimes, microfinance is not the right answer. If there is no real chance that the business proposal can work or generate a social or environmental return, the CDFI or credit union would have to turn down the loan application.

People who take microfinance loans and are unwilling to repay them may feel resentful if the lender takes action against them.

As with any financial investment, social investments can be risky. Whether a loan or a grant, there is no guarantee you will achieve the results you are aiming for. You must review your plans and be clear about how much risk you are willing to take on and how you will learn from the successes and failures of your investments.

Some people or local areas may object to lending on moral or religious grounds. We will only work with reputable, community-based lenders such as CDFIs and will do our best to make lending available that complies with ethical and religious principles.



How does microfinance work and who administers the loans?

There are two types of organisations providing microfinance, using social investment:

Community development finance institutions: (CDFIs) lend money to individuals and businesses that struggle to access 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. CDFIs' aims are not to make a private profit but to support communities by providing affordable finance that would not otherwise be available.

Credit Unions: these are run by their members for their members and offer savings accounts, loans and other financial services. They serve everyone but they often have a special mission to serve low-income communities. They are regulated by the Financial Services Authority and are members of the Financial Services Compensation Scheme. Credit unions are member-owned co-operatives and any profits are shared by their members or re-invested in the credit union.

Credit unions and CDFIs provide a range of different microfinance loans for different reasons:

- to get a new business up and running
- to buy a vehicle or other equipment
- for advertising or marketing to reach new customers
- to lease or fit out a building
- working capital, to finance the business until customers pay their bills.

How do we select a community finance organisation to work with?

If your local area wants to fund microfinance using social investment, Local Trust can help you to select a CDFI or credit union to manage the lending on your behalf. In the coming months, Local Trust will create a detailed Big Local guide to help local areas select a community finance organisation to work with.



Social investment loans are just one way that Big Local areas can spend their £1m – areas can also make grants, and purchase services.

MORE INFO

For more information on social investments, grants or services, talk to your Big Local rep. Alternatively, you can talk to the staff team at Local Trust by ringing 0207 812 5456, or emailing: info@localtrust.org.uk

This document will be developed over time with input from the people using this material. If you have thoughts on how this document can be made more useful for you, particularly if you live in one of the Big Local areas, please let us know.

Local Trust

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If you need this document in other formats or a community language please get in touch with Local Trust and we will help you.

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