

## **CABINET**

**12 JULY 2022**

### **UPDATE ON THE FORMATION OF SOUTH WEST MUTUAL (SWM)**

**Cabinet Member** Cllr Andrew Moore, Cabinet Member for Finance  
**Responsible Officer** Andrew Jarrett, Deputy Chief Executive (S151)

**Reason for Report:** To provide an update on the formation of South West Mutual.

**RECOMMENDATION:** That the Cabinet note the update.

**Financial Implications:** The £50,000 invested in this project to support the local economy bought 3,333 £15 ordinary shares. Should it succeed, the community should benefit and the Council may benefit financially through dividends. Should it fail, this will be a sunk cost.

**Legal Implications:** No equality issues identified for this report

**Risk Assessment:** Regular updates will be brought to Members to keep them informed of progress.

**Equality Impact Assessment:** No equality issues identified for this report. The project could provide a positive contribution by making banking services more readily available in the District.

**Relationship to Corporate Plan:** The proposal supports the Corporate Plan priority of Economy, encouraging business development and growth and also Community by helping the local community to access banking services, which are disappearing from the high streets across the District.

#### **1.0 Introduction/Background**

- 1.1 On 7 March 2019, Cabinet agreed to grant £50,000 towards the creation of the South West Mutual – a regional bank for inclusive growth.
- 1.2 The mutual sought initial investment in order to progress its Banking Licence application. It will then need to find an estimated £2.5m to set up operations and complete the banking authorisation process, and finally a further investment of £17.5m to capitalise the bank and enable it to commence trading.
- 1.3 The last update to Cabinet was October 2021, which fed back that little progress has been achieved largely due to Covid-19 impacting on economic conditions and the subsequent furloughing of staff at various times.
- 1.4 The report also updated members on two issues regarding the Corporate Structure and Competition Law, which consequently reduced the ability to attract additional investment. This report provides a progress update on these issues and updates on other developments.

## 2.0 The latest update

### 2.1 Corporate Structure

- 2.1.1 In response to the ruling from the Financial Conduct Authority (FCA) that determined cooperative societies registered under the Cooperative and Community Societies Act 2014 were not able to issue shares at different prices, the corporate structure of the Mutual has been reviewed based on advice from PricewaterhouseCoopers (PwC) and Anthony Collins Solicitors.
- 2.1.2 The Mutual is instead looking to register under the Companies Act 2006, which also provides the following features:
- Corporate purpose defined as promoting the 'common good', not private profit;
  - Mutual ownership and governance are embedded through one-member one-vote, but unlike many Mutuals, equal membership is given to customers, workers and shareholders. An elected Members Council also includes representatives from community, social and environmental organisations to represent the voices of non-members and future generations;
  - Ability to issue shares at different prices over time to reward early-stage investors;
  - Share capital that qualifies as equity capital for the purposes of banking regulations.

### 2.2 Competition Law

- 2.2.1 Following extensive due diligence, the Mutual's Directors concluded that the application of competition law in practice creates an unacceptable level of legal risk for a bank that seeks to serve members only from a defined and published geographical area.
- 2.2.2 Instead, to manage the regional focus, SWM are proposing to apply geographical criteria to each product, rather than to the location of the customer at the time at which they first become a member.

### 2.3 Investment Capital

- 2.3.1 The financial regulations applied to Mutuals require significant initial capital to underpin its activities. The bank will require capitalisation of at least £25 million to be raised through issuing shares on which dividends will be paid, with target returns of 5%-6% per annum over the long term.
- 2.3.2 Although SWM has attracted patient investors interested in a combination of positive social and environmental impacts with sensible financial returns over a longer-term timeframe, it remains the case that venture capital investors that specialise in financing start-up ventures, that are by their nature more risky than well-established companies, seek investment returns well beyond those that it is sensible for a financial mutual to seek to deliver.

- 2.3.3 SWM are making the case to Government for them to access funds through the Dormant Assets Scheme, which takes unclaimed savings and financial assets from banks and other financial services firms and applies them to good causes.

### 3.0 **Revised Strategy – the South West Agroecology Fund (SWAF)**

- 3.1 The overall objective remains to obtain a full banking licence, and to introduce a full range of high street banking services to households and businesses in the region over time. The business model remains closely aligned to that originally presented to investors with modifications to take account of changes in banking technology and consumer trends.
- 3.2 However, in response to these issues, the Board has adopted a revised strategy of introducing banking services in stages, starting with a business loan fund aimed specifically at smaller farms that want to invest in nature friendly farming practices – the South West Agroecology Fund (SWAF) (**see Appendix 1**).
- 3.3 This is a revolving £20m business loan fund to finance the transition to nature friendly farming practices. Agroecology is a nature friendly approach to agriculture that seeks to eliminate chemical inputs, diversify production, improve biodiversity, ecosystem and soil health, reduce carbon emissions and maximise production synergies within the farm.
- 3.4 This strategy has a number of benefits including commencing trading much sooner by initially launching services that do not require a banking licence. A transition to agroecology in the UK could also:
- Reduce carbon emissions by upwards of 70%
  - Support species abundance on and beyond farms, restore ecosystems, rebuild soil health and improve water quality
  - Grow enough healthy and sustainable food for all
  - Support rural business and livelihoods
- 3.5 Research has identified that there is insufficient bank finance available for food and farming businesses making significant changes to their production methods, sourcing policies, retail and distribution channels to transition away from intensive agriculture, particularly smaller farms, new entrants and tenant farmers. It is thought that this will therefore fill a funding gap.
- 3.6 The next step is to complete legal and operational preparations and raise finance to launch the South West Agroecology Fund in late 2022 / early 2023. SWM is currently developing the operating and legal structure for the fund and, subject to securing sufficient investment, plans to launch SWAF in late 2022 / early 2023.
- ### 4.0 **Banking Business Model**
- 4.1 Other elements of the business model have been revised in the light of detailed market research, due diligence, and developments in the banking industry, including evolving consumer trends and technological advances.

- 4.2 Branches - The evolution towards digital banking services has accelerated as a result of the pandemic. At the same time, government and industry initiatives have been launched to maintain access to cash and branch banking services through Bank Hubs and Post Office access. In this context, launching with a cash handling branch network undermines the commercial viability of the proposition. Instead SWM plan to introduce a network of face-to-face customer service points over time to augment digital and telephone banking channels.
- 4.3 Technology – SWM are constantly reviewing banking technology providers as the market is developing rapidly. The current configuration offers greater functionality and flexibility than the technology providers and solutions described in the Founder Share Offer Document, which are unlikely to be the ones selected.
- 4.4 Timetable – For the reasons set out above, the target launch dates and milestones set out in the Founder Share Offer Document are no longer valid.

## 5.0 Latest Summary Financial Position

- 5.1 The past three years summary financial information for South West Mutual Limited is set out below. The most recent year is in the process of being independently audited. The previous two years are extracted from the audited financial statements.

	March 2022	March 2021	March 2020
	£'000	£'000	£'000
	Unaudited	Audited	Audited
<b>Grants and other operating income</b>	<b>(41)</b>	<b>(179)</b>	<b>(211)</b>
Staff and directors	137	241	343
Consultants and business services	37	115	41
Marketing, market research, events and travel	9	27	40
Office and administrative costs, including depreciation	13	14	22
Audit and accountancy	6	13	15
	<b>202</b>	<b>410</b>	<b>461</b>
<b>Deficit for the year</b>	<b>161</b>	<b>231</b>	<b>250</b>
Share capital	(720)	(645)	(510)
Cumulative deficits	709	548	318
<b>Net assets</b>	<b>11</b>	<b>97</b>	<b>192</b>

- 5.2 Since the year end a further £20,000 in grant funding has been received, and further grant applications are in progress alongside discussions with potential investors in SWAF.
- 5.3 SWM was cited in the Government's Levelling Up White Paper as an example of the local financial institutions needed to drive regional prosperity. It is therefore hoped that this will lead to attracting and accessing greater funding.

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**Circulation of the Report:** Cabinet Members

**List of Background Papers:** Previous Cabinet report (October 2021)