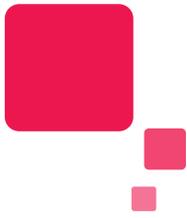


# SME Finance Monitor

Q2 2015: Management Summary

An independent report by  
BDRC Continental, September 2015



**OVERVIEW:** The Q2 2015 report continues and confirms the trends seen in recent waves. SMEs reported a range of positive indicators about themselves including for profitability, risk rating and credit balances held. Success rates for those who had applied for new/renewed loan or overdraft finance were at some of the highest levels seen, especially for overdrafts and this improvement includes groups who have previously found it harder to access finance, such as smaller businesses and those applying for the first time. Use of and demand for finance remained limited overall but the half of all SMEs now meeting the definition of a Permanent non-borrower (with little apparent appetite for finance now or in the future) may be masking signs of increased appetite for finance amongst remaining SMEs.

**CONTEXT: SMEs report a range of positive indicators about their business in terms of profitability, credit balances, and risk rating and see limited barriers for the future:**

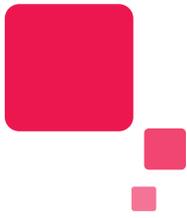
General context	
An increasing proportion of SMEs reported making a profit	80% of SMEs interviewed in Q2 2015 reported making a profit in their last trading period (excluding DK). This has increased steadily over time (it was 69% in Q2 2013)
More SMEs held over £5,000 in credit balances	Almost all SMEs hold some credit balances. In H1 2015, 40% of all SMEs held more than £5,000 in credit balances, up from 32% in 2011. The higher the credit balances held, the less likely an SME is to have an overdraft
Fewer SMEs received injections of personal funds	26% of SMEs in Q2 2015 reported an injection of personal funds, and this was as likely to have been a choice (13%) as something they had to do (13%). The proportion receiving an injection of personal funds has declined over time (42% received an injection of funds in 2012) primarily due to fewer SMEs feeling that they 'had' to put funds in
SMEs reported fewer credit issues and an improving credit profile	7% of SMEs self-reported a credit issue in Q2 2015. This was lower than in previous years (10% in Q2 2013). The proportion of SMEs with a 'worse than average' risk rating has stabilised having declined from a peak of 56% in Q2 2013 to 45% in Q2 2015
Looking forward, fewer SMEs saw the economic climate as a major barrier...	From a peak of 37% at the start of 2012, the proportion of SMEs seeing the current economic climate as a major barrier has declined steadily and was 14% in Q2 2015. For SMEs with employees, 'legislation and regulation' is now just as much of a barrier as the economic climate (11% overall). 68% of SMEs saw none of the factors tested as a major obstacle

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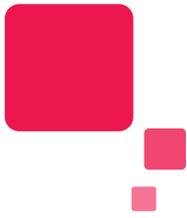
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...or felt that access to finance was a barrier	5% rated access to finance as a major barrier and this has also declined over time. Those with any future appetite for finance were more likely to see it as a barrier (13%) but this is also lower than in previous waves
4 in 10 SMEs expected to grow	43% of SMEs planned to grow. This has been stable over recent quarters but slightly lower than in 2012-13 when around half planned to grow, due to the lower and steady growth aspirations of 0 employee SMEs (39% in Q2 2015 v 55% of those with employees)



**APPLICATIONS FOR NEW/RENEWED LOAN & OVERDRAFTS: 79% of all applications made in the 18 months to Q2 2015 resulted in a facility. Both overall success rates and those for overdrafts and loans individually continue to show improvement, including for first time applicants and those seeking new funding:**

The outcome of applications	
79% of all applications in the last 18 months resulted in a facility	The success rate for new/renewed loan and overdraft facilities continued to improve over time. 79% of applicants ended the process with a facility in the 18 months to Q2 2015, compared to 67% for the 18 months to Q4 2013
Success rates for new money improved	<p>Almost all loan/overdraft <u>renewal</u> applications had been successful (96% for the 18 months to Q2 2015) and this has changed little over time. Success rates for <u>new money</u> remained somewhat lower (67% for the 18 months to Q2 2015) but have improved steadily since Q3 2013</p> <p>As before, those applying for new money for the first time were less likely to have been successful (58% for applications to Q2 2015) than those who had borrowed before (74%) but success rates for both groups are higher than in 2013</p>
84% of overdraft applicants were successful, the highest proportion recorded to date	<p>84% of overdraft applications made in the 18 months to Q2 2015 resulted in a facility (72% were offered what they wanted and took it while 12% had their facility 'after issues')</p> <p>The proportion of overdraft applicants who have been successful has improved steadily over time (it was 72% for the 18 months to Q2 2013). This improvement includes SMEs previously less likely to be successful such as smaller SMEs, those with a worse than average risk rating and first time applicants (where 62% were successful up from 36% in the 18 months to Q2 2013)</p>
7 in 10 loan applicants were successful and this has also improved over time	<p>69% of loan applications made in the 18 months to Q2 2015 resulted in a facility (55% were offered what they wanted and took it while 14% had their facility 'after issues')</p> <p>The proportion of loan applicants who have been successful has also improved steadily over time (it was 56% for the 18 months to Q2 2013). As with overdrafts, this improvement includes SMEs previously less likely to be successful such as smaller SMEs and first time applicants (where 53% were successful up from 40% in the 18 months to Q2 2013)</p>
Applying is often a 'low effort' experience, especially for overdrafts	<p>73% of successful overdraft applicants in the 18 months to Q2 2015 described the process as 'low effort', increasing to 78% of those who were offered the facility they wanted and took it (v 43% of those who had their overdraft after issues)</p> <p>Amongst successful loan applicants 55% described it as 'low effort'. Those who were offered the facility they wanted were much more likely to rate the experience as 'low effort' (64%) than those who had their loan facility after issues (17%)</p>



**FINANCIAL APPETITE:** There are a number of indicators that use of / demand for finance remains subdued overall. Use of external finance remains lower than previously seen across all sizes of SME, notably for the core forms of finance, with half of SMEs meeting the definition of a Permanent non-borrower. 7 in 10 SMEs aim to pay down any existing debt and then remain debt free: a quarter of all SMEs might be described as ‘debt averse’ while a third would still be prepared to use external finance to help the business grow and develop. Amongst those who are not PNBs though there are some signs of increased financial activity:

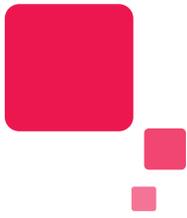
Financial appetite	
Use of external finance remained lower than in previous years	36% of SMEs were using external finance in Q2 2015. This was stable after previous declines (having been 46% in 2011), with this decline seen across all sizes and risk rating of SME
Solus use of ‘core’ forms of finance have been in notable decline	<p>Between 2011 and Q2 2015, use of ‘core’ forms of finance (loans, overdrafts and/or credit cards) declined from 39% to 28% of all SMEs. This was due primarily to a decline in the use of overdrafts (from 26% to 16%, albeit currently stable). The proportion of SMEs who <u>only</u> used ‘core’ finance also declined over this period from 29% to 20% of all SMEs, driving the decline in the use of finance overall</p> <p>17% of SMEs in Q2 2015 used one or more of the other forms of finance specified (leasing, invoice finance etc) and their use has been more stable over time</p>
Other sources of finance are stable or declining slightly over time – two thirds of SMEs use any ‘business funding’	<p>‘Business funding’ comprises any use of external finance (described above), trade credit and/or injections of personal funds</p> <p>33% of SMEs received trade credit from their customers and two thirds of them (the equivalent of 22% of all SMEs) said that they needed less external finance as a result</p> <p>A declining proportion of SMEs (26% in Q2 2015) reported an injection of personal funds into the business</p> <p>Including the receipt of trade credit and injections of personal funds alongside external finance saw 63% of SMEs using business funding YE Q2 2015, compared to 37% of SMEs using only external finance. The biggest uplift was seen for those with 0 employees (from 32% to 59%)</p>

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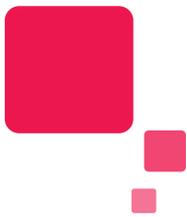
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<p>Half of SMEs were 'Permanent non-borrowers'</p>	<p>49% of SMEs met the definition of a 'Permanent non-borrower' in Q2 2015 and this has increased over time, from 34% in 2011. Smaller SMEs remained more likely to be a PNB (53% of those with 0 employees in Q2 2015) but a quarter of SMEs with 10-249 employees were PNBs</p> <p>New analysis of this growing portion of the market shows that PNBs are performing well (in terms of profitability, risk rating and past growth) but are not necessarily as ambitious as other businesses (in terms of innovation and planned future growth)</p> <p>If PNBs using trade credit or receiving injections of personal funds were excluded (to match the business funding definition above) then the proportion of PNBs would drop to 29% of SMEs</p> <p><u>Excluding</u> the PNBs increases the proportion of remaining SMEs using external finance to 70% for 2015 to date, somewhat higher than in previous years (ranging from 65-68% for 2012-14)</p>
<p>Three quarters of SMEs aimed to pay down debt and remain debt free</p>	<p>73% of SMEs interviewed YEQ2 2015 agreed that their aim was to pay down any existing debt and then remain debt free, and this varied little by size of business. Meanwhile 43% agreed that they would be happy to use external finance to help the business grow and develop, increasing by size of SME</p>
<p>28% of SMEs were 'debt averse' while 37% might borrow in the right circumstances</p>	<p>Combining the two statements above, 28% of all SMEs wanted to pay down debt and would not be happy to borrow to help the business grow – these might be described as 'debt averse' and this was more likely amongst smaller SMEs. 37% of all SMEs also wanted to pay down debt, but would be happy to borrow to finance growth, and so might apply in the right circumstances, and this was more likely amongst larger SMEs</p>



**BORROWING EVENTS IN LAST 12 MONTHS: 16% of SMEs had experienced any form of borrowing ‘event’. There were fewer ‘Would-be seekers’ of finance and the proportion of ‘s’ increased again:**

Borrowing events	
7% applied for a new/renewed loan or overdraft	YEQ2 2015, 7% of SMEs reported a Type 1 event (an application for a new/renewed loan or overdraft) in the previous 12 months. Larger SMEs were more likely to have applied – 5% of 0 employee SMEs reported such an application compared to 13% of those with employees
16% had experienced any loan or overdraft borrowing ‘event’	YEQ2 2015, 17% of all SMEs reported any borrowing event in the previous 12 months including the automatic renewal of an overdraft facility and this is stable over recent quarters, but lower than the 1 in 4 reporting an event when the Monitor started in 2011
Few SMEs had wanted to apply but felt something had stopped them	YEQ2 2015, 3% of SMEs were ‘Would-be seekers’ of finance who would have liked to apply for a loan/overdraft but felt that something stopped them. This proportion has declined over time (it was 6% in Q2 2013 compared to 2% in Q2 2015). Discouragement (almost all of it indirect) and the process of borrowing remained the two main barriers to application for this group
8 in 10 SMEs have been ‘Happy non-seekers’ of finance	YEQ2 2015, 80% of SMEs were ‘Happy non-seekers’ of finance for the 12 months prior to interview. The proportion of SMEs in this group has increased over time (in Q2 2013 it was 76% increasing to 82% in Q2 2015)
There is some limited evidence of an increase in appetite once the PNBs are excluded	49% of SMEs in Q2 2015 met the definition of a PNB and they are therefore a major influence on the overall use of and appetite for finance. Excluding them from this analysis increases the proportion of SMEs reporting a borrowing ‘event’ in 2015 to date to 33%, somewhat higher than the 28% reported for both 2013 and 2014 and almost in line with 2012 (35%)



**FUTURE APPETITE FOR FINANCE:** Future appetite for finance remains flat but where an application is planned there is confidence that their bank will agree to lend (albeit future applicants are not as confident as current success rates indicate), and higher awareness of various initiatives to help them. Fewer SMEs think they will be ‘Would-be seekers’ of finance, which leaves most, as before, to be future ‘Happy non-seekers’ of finance:

Looking ahead	
Future applications remain limited but with signs of improvement once the PNBs are excluded	<p>11% of SMEs planned to apply for new/renewed finance in the 3 months after Q2 2015, at the lower end of the narrow range seen over recent years (12-15%). This is driven by the views of those with 0 employees (9% plan to apply) with a higher appetite for finance amongst those with employees (16%)</p> <p>Excluding the PNBs sees an increase in the proportion of remaining SMEs planning to apply to 24% for 2015 to date, somewhat higher than in previous years (21% planned to apply in 2012)</p>
Confidence of success increased amongst future applicants but the confidence ‘gap’ remained	49% of potential future applicants were confident that the bank would agree to their request. There remains a gap between confidence and actual success rates for both renewals (57% confident versus a current success rate of 96%) and for new money (35% confident versus a current success rate of 67%)
The economic climate remains a barrier to future applications	10% of SMEs in Q2 2015 were ‘Future would-be seekers’. This group is decreasing in size over time (in Q2 2013, 19% of SMEs were FWBS) with the current economic climate still the main barrier to an application, notably where no immediate need for finance was identified
8 in 10 SMEs expected to be future ‘Happy non-seekers’ of finance	In Q2 2015, 79% of SMEs expected to be ‘Happy non-seekers’ of finance in the following 3 months. Over time, more SMEs have met this definition – in Q2 2013, 67% were ‘Future happy non-seekers’
Half of SMEs were aware of specific finance initiatives/bodies	A third of SMEs (32%) believed they were aware of any government or other initiatives to help SMEs access finance. Once prompted with 5 specific schemes/bodies, awareness increased to 53%. Larger SMEs were more likely to be aware (59% of those with 50-249 employees) as were those planning to apply for external finance in the next 3 months (58%)

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<p>Awareness over time of specific initiatives remained unchanged</p>	<p>Across all the initiatives tested in Q2 2015, individual awareness was highest for Start-up Loans (40%) and the Funding for Lending Scheme (24%). Where initiatives have been tracked over time, awareness is typically stable as is the proportion of SMEs contacted by banks to express a willingness to lend</p>
<p>Awareness of crowd funding continued to increase</p>	<p>37% of SMEs (excluding the Permanent non-borrowers) in 2015 to date were aware of crowd funding, including 1% who were using this form of finance</p> <p>In contrast to the other initiatives tracked over time, awareness of crowd funding has increased steadily over time (22% were aware of crowd funding in the first half of 2014)</p>
<p>1 in 3 of those who have heard of crowd funding would consider it as a form of finance</p>	<p>Three in ten of those who have heard of crowd funding said that they would consider using it in future (the equivalent of 11% of all SMEs excluding the PNBs). As awareness has increased, the proportion of those aware who would consider this type of funding has not changed</p>

