

## 2. Management summary



### **This report covers**

the borrowing process from the SME's perspective, with detailed information about those who have, or would have liked to have been, through the process of borrowing funds for their business. Each chapter reports on a specific aspect of the process, dealing with different aspects of SME finance.



In the run up to the referendum result, demand for finance amongst SMEs continued to be muted, with many saying they preferred to self-fund any future growth:

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<b>A third of SMEs were using external finance</b>	<p>36% of SMEs were using external finance (YEQ2 2016). This has been stable over recent quarters but remained lower than in previous years (in 2012, 44% were using external finance), primarily due to lower levels of use of core finance (loans, overdrafts and/or credit cards).</p> <p>As in previous reports, use of external finance increased by size of SME from 31% of those with 0 employees to 62% of those with 50-249 employees.</p>
<b>More SMEs qualified as Permanent non-borrowers than used external finance</b>	<p>46% of SMEs met the definition of a Permanent non-borrower with little apparent appetite for external finance (YEQ2 2016). As use of external finance has declined, this group has increased in size from 34% of SMEs in 2012 to 48% in the first half of 2016.</p> <p>Whilst smaller SMEs remained more likely to be PNBs (50% of those with 0 employees YEQ2 2016) just over a quarter of SMEs with 10-249 employees also met the definition.</p>
<b>Demand for new or renewed loans and overdrafts remained muted</b>	<p>6% of SMEs had applied for a new or renewed loan or overdraft in the 12 months prior to interview (YEQ2 2016). This has declined from 11% in 2012, across all size bands, risk ratings and once the PNBs were excluded.</p>
<b>Many SMEs appeared to prefer self-funding</b>	<p>80% of SMEs agreed that their current plans were based on what they could afford to fund themselves (YEQ2 2016).</p> <p>In new questions for 2016, 71% agreed that they would accept a slower growth rate they funded themselves rather than borrow to grow more quickly and 47% agreed that they never thought about whether to use (more) finance in the business. In all instances smaller SMEs were more likely to agree.</p>
<b>Being prepared to borrow to grow is linked to current use of finance</b>	<p>44% of SMEs agreed that they were happy to use external finance to help the business grow (YEQ2 2016), with limited variation by size (42% of those with 0 employees to 54% of those with 50-249 employees).</p> <p>Those who were already using external finance were much more likely to agree with this statement (57%) than those who weren't (37%). Overall, a quarter of all SMEs (24%) were not currently using external finance but said that they would be prepared to borrow in future while almost twice as many (40%) were neither using finance nor would they be prepared to borrow in future.</p>



Demand for external finance may also be affected by other funding being available such as retained profits, cash balances and trade credit:

<b>Most SMEs reported making a profit</b>	81% of SMEs reported making a profit in their last 12 months trading (YEQ2 2016 excluding DK answers). This proportion has improved steadily from 2012 when 69% reported making a profit and also across size bands.
<b>Most also hold credit balances, which can reduce their need for external finance</b>	<p>Almost all SMEs hold some credit balances. The proportion of SMEs holding more than £10,000 in credit balances increased from 16% to 24% between 2012 and 2015 but was slightly lower (21%) in the first half of 2016.</p> <p>Most of those who held such sums said that it reduced their need for external finance and analysis showed that the proportion of SMEs with £10,000 or more who also used <u>any</u> external finance had declined from 51% in 2012 to 45% in the first half of 2016.</p>
<b>A third use trade credit, which can also reduce the need for external finance</b>	<p>A consistent 32% of SMEs regularly purchased goods or services from other businesses on credit. The proportion increased from 26% of those with 0 employees to 58% of those with 50-249 employees and was also higher for those also using external finance (43% v 24% of those not using external finance).</p> <p>Two thirds of those who received trade credit said that it reduced their need for external finance and this varied little by size of SME.</p>
<b>Fewer SMEs have felt that they had to inject personal funds</b>	<p>28% of SMEs reported an injection of personal funds into the business (YEQ2 2016). This proportion has varied little over recent quarters having previously fallen from 43% in 2012 to 29% in 2014.</p> <p>This decline was primarily due to fewer SMEs feeling that they <u>had</u> to inject personal funds (25% in 2012 to 15% in 2014 – and 13% YEQ2 2016).</p>
<b>Use of any business funding remained stable</b>	<p>While 36% of all SMEs used external finance, this increased to 63% using business funding when trade credit and injections of personal funds were added in.</p> <p>Use of crowd funding remained limited (1% of all SMEs).</p>



Most SMEs had been Happy non-seekers of finance. Those applying for new or renewed loan or overdraft finance remained likely to end the process with a facility, with satisfaction clearly impacted by whether they had been offered the facility they wanted or not:

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<b>8 in 10 SMEs were Happy non-seekers of external finance</b>	<p>81% of SMEs met the definition of a Happy non-seeker of finance (YEQ2 2016) and that proportion has increased over time, from 68% of SMEs in 2012 to 83% in the first half of 2016.</p> <p>Very few SMEs felt that something had stopped them applying for a facility – 4% met this definition of a Would-be seeker (YEQ2 2016), down from 10% in 2012.</p> <p>15% reported a borrowing event which includes those with an automatically renewed overdraft (YEQ2 2016) and this has also declined over time from 23% of SMEs in 2012 to 14% in the first half of 2016.</p>
<b>Would-be seekers were more likely to hope for a different relationship with their bank</b>	<p>In a new question, two thirds of SMEs in the first half of 2016 described the relationship with their main bank as ‘fine, but transactional’. 22% said that they had a ‘strong working relationship’ with their bank and this was much more likely to be the case for larger SMEs (51% of those with 50-249 employees compared to 19% of those with 0 employees).</p> <p>12% would have liked a more active relationship with their bank. This was more likely to be the case for smaller SMEs and in particular for those who had been Would-be seekers of finance (28%).</p>
<b>8 in 10 applications for new or renewed finance resulted in a facility</b>	<p>81% of all loan and overdraft renewals reported to date for the 18 months to Q2 2016 resulted in a facility. This proportion has increased over time, from 69% of applications in the 18 months to Q4 2012.</p> <p>Almost all renewals of loans and overdrafts were successful, with no change over time. The increase in overall success rate was therefore due to the increased success rate for new money applications (54% to 66%) and for first time applicants in particular (41% to 61%) although this was driven by first time overdraft applicants much more than by first time loan applicants.</p>
<b>Overdraft applicants remained more likely to be successful than loan applicants</b>	<p>84% of overdraft applicants and 72% of loan applicants in the 18 months to Q2 2016 ended the process with a facility.</p> <p>In both instances success rates have improved over time. In the 18 months to Q4 2012, 74% of overdraft applications and 59% of loan applications were successful.</p> <p>Early indications for 2016 suggest some weakening of success rates, possibly driven by the profile of applicants and this will be followed up in future reports.</p>

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**Those offered what they wanted were very satisfied and rated the process a 'low effort' experience**

In a new question for 2016, more than 9 in 10 of loan and overdraft applicants offered the facility they wanted said that they had been satisfied with the application process itself and most (8 in 10 of these overdraft applicants and 6 in 10 of these loan applicants) rated the process as 'low effort'.

Those experiencing any other outcome (having a facility after issues, taking other funds or having no facility) were much less likely to have been satisfied with the application process (15% of such overdraft applicants and 17% of such loan applicants). Base sizes are limited for this new question and further analysis will be provided as more data is gathered.



Looking forward, larger SMEs became more concerned about the economic climate and political uncertainty during the referendum campaign. Whilst levels of past growth have remained consistent, levels of future growth were somewhat less certain. Future appetite for finance remained stable, with most confident the bank would say yes (whether they planned to apply or not):

<b>Two thirds of SMEs did not identify any factor as a 'major barrier' to their business</b>	<p>In Q2 2016, 68% of SMEs did not identify any of the potential obstacles tested as 'major barriers'. As in previous waves, the most likely to be mentioned were the economic climate (rated a major obstacle by 13% of SMEs), legislation and regulation (11%) and political uncertainty/government policy (10%).</p>
<b>However, larger SMEs, or those with plans to grow or borrow had concerns</b>	<p>Those with plans to grow (38%) or any future appetite for finance (47%) were more likely to identify one or more obstacles than those with no such plans (28% and 27% respectively).</p> <p>Over the referendum campaign the proportion rating either the 'Economic climate' or 'Political uncertainty' as 'major barriers' did not change much overall but doubled for those with 50-249 employees: 14% rated the economic climate a major barrier in Q2 2016 up from 8% in 2015, and 16% rated political uncertainty a major barrier in Q2 2016 up from 7% in 2015</p>
<b>Fewer SMEs are planning to grow</b>	<p>In Q2 2016, 41% of SMEs were planning to grow in the next 12 months, ranging from 38% of those with 0 employees to 60% of those with either 10-49 or 50-249 employees.</p> <p>Over time, the proportion planning to grow has fallen from 49% in 2013 to 43% for the first half of 2016, due to lower growth expectations amongst the smallest and largest SMEs.</p>
<b>The proportion planning to apply for finance has changed little over time</b>	<p>11% of SMEs in Q2 2016 planned to apply for new or renewed finance in the 3 months after interview. This has varied little over time: 14% of those interviewed in 2012 and 2013 planned to apply and then 13% in 2014, 2015 and the first half of 2016.</p> <p>This is due to a relatively stable appetite for finance amongst the 0 employee SMEs. Amongst those with employees, future appetite for finance has declined somewhat (by between 3 and 6 percentage points).</p>

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**Those with no plans to apply are typically confident the bank would say yes if asked**

All SMEs are now asked how confident they would be that the bank would agree to a (potentially hypothetical) application for finance.

Amongst those planning to apply for bank finance in H1 2016, 50% were confident the bank would say yes, maintaining the increase seen from 2012, when 42% were confident.

Confidence amongst Future happy non-seekers of finance (who made up 75% of SMEs in the first half of 2016) for a hypothetical application was higher at 67% than amongst those planning to apply to a bank.

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**Future would-be seekers appear less confident about applications generally**

Future would-be seekers made up 12% of SMEs in the first half of 2016, down from 23% in 2012.

The FWBS were less confident than other groups that their bank would agree to lend if they were to apply (44%).

They were also less confident about assessing the products and services available at their main bank (58% v 69% overall), or at another bank (49% v 61% overall) and less confident about making an application for funding to another bank (53% v 60% overall).

The Future happy non-seekers with no plans for finance were typically the most confident in all of these scenarios, ahead of those actually planning to apply.