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 loan or overdraft funding for their business. Each chapter reports on a specific aspect of the process, dealing with different aspects of SME finance.

In 2016 demand for finance amongst SMEs remained muted, with half meeting the definition of a Permanent non-borrower and many saying they preferred to self-fund any future growth:

A third of SMEs were using external finance	37% of SMEs were using external finance (YEQ4 2016). There was some variation within 2016, but overall levels of finance remained in line with 2015 and below levels previously seen (in 2012, 44% were using external finance). As in previous reports, use of external finance in 2016 increased by size of SME from 33% of those with 0 employees to 64% of those with 50-249 employees.
More SMEs qualified as Permanent non-borrowers than used external finance	47% of SMEs met the definition of a Permanent non-borrower with little apparent appetite for external finance (YEQ4 2016). This is also unchanged from 2015, and remains higher than previously seen (34% in 2012). Whilst smaller SMEs remained more likely to be PNBs (50% of those with 0 employees YEQ4 2016) a third of SMEs with employees also met the definition (37%).
Demand for new or renewed loans and overdrafts remained muted	5% of SMEs had applied for a new or renewed loan or overdraft in the 12 months prior to interview (YEQ4 2016). This is the lowest level recorded to date on the Monitor, having been 11% in 2012 and 7-8% for 2013-15. The decline was seen across all size bands, risk ratings and once the PNBs were excluded.
Many SMEs appeared to prefer self-funding	A stable 80% of SMEs agreed that their current plans were based on what they could afford to fund themselves (YEQ4 2016) with limited variation by size (81% of those with 0 employees to 65% of those with 50-249 employees). 71% agreed that they would accept a slower growth rate they funded themselves rather than borrow to grow more quickly, with levels of agreement declining with size of business (71% of those with 0 employees to 55% of those with 50-249 employees). In a new statement for H2 2016, half of SMEs (49%) agreed that a fall in the cost of credit would *not* make them any more likely to consider applying for new finance, with little variation by size.
Being prepared to borrow to grow is linked to current use of finance	A stable 43% of SMEs agreed that they were happy to use external finance to help the business grow (YEQ4 2016), with little variation by size (41% of those with 0 employees to 51% of those with 50-249 employees). Those who were already using external finance remained more likely to agree with this statement (54%) than those who weren't (36%). Overall, 1 in 10 of all SMEs (11%) were planning to grow in the next 12 months and although not currently using finance would consider it to help the business grow, providing an indication of possible future demand for finance.

Demand for external finance may also be affected by other funding being available such as retained profits, cash balances and Trade Credit. SMEs reported a stable position for 2016:

Most SMEs reported making a profit	80% of SMEs reported making a profit in their last 12 months trading (YEQ4 2016 excluding DK answers), unchanged from 2015. This proportion has improved steadily from 2012 (when 69% reported making a profit) and also across all size bands.
Most also hold credit balances, which can reduce their need for external finance	Almost all SMEs hold some credit balances. The proportion of SMEs holding more than £10,000 in credit balances increased from 16% to 25% between 2012 and 2015 but was slightly lower (22%) in 2016, due to the 0 employee SMEs being somewhat less likely to hold such sums. 8 in 10 of those who held £10,000 or more 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 any external finance had declined from 51% in 2012 to 46% in 2016.
A third used Trade Credit, which can also reduce the need for external finance	A consistent 33% of SMEs regularly purchased goods or services from other businesses on credit. 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.
Fewer SMEs have felt that they had to inject personal funds	28% of SMEs reported an injection of personal funds into the business (YEQ4 2016). This proportion has remained stable since 2014, and below the 43% injecting funds in 2012. The decline has been driven by fewer SMEs feeling that they 'had' to inject funds, from 25% of SMEs in 2012 to 11% in 2016.
Use of any business funding remained stable	While 37% of all SMEs used external finance, this increased to 63% using 'business funding' when Trade Credit and injections of personal funds were added in. Use of crowd funding remained limited (1% of all SMEs).
Those with a business mentor were more likely to have grown	1 in 8 SMEs had a business mentor, increasing by size of SME from 14% of 0 employee SMEs to 24% of those with 50-249 employees. Analysis showed that SMEs with a mentor were more likely to have grown (50% v 39% of those without a mentor) and also to be planning to grow (61% v 43% of those without a mentor) and this was true across all sizes of SME, especially for those with 0 employees. SMEs with mentors were also more likely to use external finance (45% v 37%) but were only slightly more likely to be planning to apply for finance (16% v 13%).

8 in 10 of those who applied for loans or overdrafts were successful, with little evidence of any change to recent success rates. Most SMEs continued to meet the definition of a Happy non-seeker of finance.

8 in 10 SMEs were Happy non-seekers of external finance	13% reported any borrowing 'event' including automatically renewed overdrafts (YEQ4 2016). This has declined over time from 23% of SMEs in 2012 and 16-17% for 2013 to 2015. 84% of SMEs met the definition of a Happy non-seeker of finance (YEQ4 2016) and that proportion has increased over time, from 68% of SMEs in 2012.
Very few SMEs have been Would be seekers of loans, overdrafts, or other forms of finance	The proportion of Would-be seekers of finance has declined over time, from 10% in 2012 to 2% of all SMEs in 2016. Including potential applications for other forms of finance (such as leasing) does not increase this proportion. Discouragement remained the main barrier for smaller WBS while larger ones were more likely to cite the process of borrowing. Would-be seekers were more likely than other SMEs to have seen an injection of personal funds into their business (60%) in 2016 and to wish that they had a more active relationship with their bank (34%).
A consistent 8 in 10 applications for new or renewed finance resulted in a facility	83% of all loan and overdraft renewals reported to date for the 18 months to Q4 2016 resulted in a facility. This proportion is unchanged from the 82% who were successful in the 18 months to Q4 2015 and remains higher than previous periods (69% of applications were successful in the 18 months to Q4 2012). Almost all renewals of loans and overdrafts were successful, with no change over time. Overall success rates for new money increased from 49% in the 18 months to Q4 2013 to 70% in the 18 months to Q4 2015 and have remained stable since (71% for the 18 months to Q4 2016).
Overdraft applicants remained more likely to be successful than loan applicants	86% of overdraft applicants and 74% of loan applicants in the 18 months to Q4 2016 ended the process with a facility. Overdraft success rates improved from 74% for the 18 months to Q4 2013 to 86% for the 18 months to Q4 2015 and have been stable since. Success rates for first time overdraft applicants also increased between 2013 and 2015 (34% to 66%) and have been stable since (currently 66% for the 18 months to Q4 2016). Loan success rates improved from 58% in the 18 months to Q4 2013 to 74% in the 18 months to Q4 2015 and have been stable since. There has been a smaller and less consistent increase in success rates amongst first time loan applicants (45% for the 18 months to Q4 2013 and 51% for the 18 months to Q4 2016). 97% of overdraft applicants and 93% of loan applicants in the 18 months to Q4 2016 said that their facility had been made available 'in good time' for when it was needed.

Looking forward, larger SMEs and those who trade internationally have become more concerned about the economic climate and political uncertainty. Whilst levels of past growth 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):

7 in 10 SMEs did not identify any factor as a 'major barrier' to their business	In Q4 2016, 70% 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), political uncertainty/government policy (12%) and legislation and regulation (10%). These have changed very little over time.
However, larger SMEs, and international SMEs had more concerns	During 2016 the proportion rating either the 'economic climate' or political uncertainty as major barriers did not change much overall but almost doubled for those with 50-249 employees: 13% rated the economic climate a major barrier in Q4 2016 up from 8% in 2015, and 15% rated political uncertainty a major barrier in Q4 2016 up from 7% in 2015. A more dramatic increase was seen amongst SMEs who trade internationally, notably those who both import and export: 35% rated the economic climate a major barrier in Q4 2016, up from 17% in 2015 and 32% rated political uncertainty a major barrier in Q4 2016 up from 8% in 2015.
Over time, fewer SMEs have planned to grow	Over time, the proportion of SMEs planning to grow has fallen from 49% in 2013 to 43% for 2016 as a whole. Over the same period the proportion of SMEs (excluding Starts) that had *achieved* growth remained stable at 40%. During 2016 there was some variation in the proportion of SMEs expecting to grow, from 45% in Q1 to 41% for both Q2 and Q3, before an increase in Q4 to 47%. This variation was caused by the 0 and 1-9 employee SMEs. Those who import and export were more likely to be planning to grow (70% for 2016 as a whole) and these growth expectations were in line with 2015. This was also the case for those who only import (63% planned to grow in 2016) while those who only export were less likely to be planning to grow (49% v 59% in 2015).
The proportion planning to apply for finance has changed little over time thanks to the 0 employee SMEs	12% of SMEs in 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 and 2015. 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 since 2013 by between 5 and 6 percentage points.

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Those with no plans to apply were 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 Q4 2016, 59% were confident the bank would say yes, maintaining the increase seen from 2012, when 42% were confident. This increase has been seen across both larger and smaller potential applicants. Future happy non-seekers of finance made up three-quarters of SMEs in 2016. Their confidence about a hypothetical application was higher in Q4 than amongst those planning to apply to a bank (72%).
Future would-be seekers appeared less confident about applications generally	Future would-be seekers made up 13% of SMEs in 2016, almost unchanged from 2015 (11%) and remaining below the 23% meeting the definition in 2012. The FWBS were less confident than the Happy non-seekers that their bank would agree to lend if they were to apply (57% in Q4 2016), but their confidence has increased since this question was first asked in Q1 2016 (when 38% were confident). They were also less confident about assessing the products and services available at their main bank (59% v 68% overall), and less confident about making an application for funding to another bank (51% v 61% overall). The Future happy non-seekers with no plans for finance were typically the most confident in these scenarios, ahead of those actually planning to apply.