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NEED FOR FUNDING

THIS CHAPTER PROVIDES

new detail on those SMEs that reported a funding need in 2020, including why the funding was needed and what steps were considered and taken to meet that need.

KEY FINDINGS

Need for funding: In 2020 overall, 9% of SMEs reported having had a need for funding, up from 3-4% in 2018-19. Analysis by quarter showed that need increased steadily during 2020, from 4% in Q1 to 14% in Q4 and across all size bands (though the increase was more limited for those with 50-249 employees).

Reasons for need for funding: In Q2 the option of 'to cope with the impact of the pandemic' was added to the list of reasons why this funding was needed. This helped to boost the proportion citing cash flow as the reason for wanting funding from 49% in 2019 to 81% Q2-4 2020, as the proportion wanting funding for business development purposes fell from 58% to 24%.

Actions considered and taken: Most SMEs with a need for funding took some initial action, with more mentions in Q2-4 2020 of speaking to their main bank (38% from 18% in 2019) and over half, 55%, speaking to either the bank, another provider or an advisor at that stage. They were also more likely to consider and then go on and make an application (80% v 57% in 2019) and for that to be at the main bank (65% from 29%), with a marked decrease in the proportion deciding to find some or all of the funding themselves (12% from 29%).

The middle section of the questionnaire, around applications made for finance, saw the most changes in the re-design for Q1 2018. As a result, this section of the report has also evolved, although where comparable data over time is still available, this has been reported.

This is the first of the three revised chapters, now looking at borrowing events in the wider finance market beyond loans and overdrafts:

- This chapter looks at whether SMEs had identified a need for external funding and what steps they took as a result of that need, including whether they applied for finance (a Type 1a borrowing event). This analysis is by interview date.
- Chapter 8 provides an overview of all borrowing ‘events’ (including Type 1a events), and the types of SME more or less likely to have had each of these events. This analysis is also by interview date.
- Chapter 9 looks specifically at the Type 1 borrowing events, the final outcome of the applications made and the impact of the application on the SME. This analysis is based on all applications made between Q3 2019 and Q4 2020 and reported in interviews conducted in the same period.

The definitions of all the borrowing events included in this report is provided at the start of the next chapter.

HAVING, AND MEETING, A NEED FOR FUNDING

Rather than being asked directly about any applications made for loans and overdrafts, from Q1 2018 respondents have initially been asked about any need for external funding in the past 12 months, in addition to any finance they already used, and irrespective of whether they acted on that need or not. Those who went on to apply for finance as a result of this funding need are defined as having had a Type 1a borrowing event later in this report.

This chapter is based on those interviewed between Q1 2020 and Q4 2020 (YEQ4 2020) who reported a need for funding in the 12 months prior to interview (ie from Q1 2019 onwards).

HAD A NEED FOR FUNDING

As the table below shows, whilst only a minority of SMEs each quarter reported a need for external funding in the previous 12 months, the proportion did increase during 2020 to 14% in Q4, the highest proportion seen to date:

Had a funding need

By date of interview

Over time – row percentages	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020
All SMEs	4%	2%	5%	3%	3%	4%	6%	11%	14%
0 employee	3%	2%	4%	2%	2%	4%	5%	11%	13%
1-9 employees	5%	5%	7%	5%	5%	6%	6%	10%	16%
10-49 employees	5%	5%	5%	5%	5%	5%	9%	11%	16%
50-249 employees	2%	4%	1%	3%	2%	4%	7%	12%	8%

Q25 All SMEs (new Q1 2018)

The table below looks at the results available over time for 2018 to 2020, across key demographics. It shows that the overall increase in 2020 to 9% was seen across all size bands and risk ratings and sectors, notably Transport and Manufacturing. 1 in 5 of those using external finance reported a need for (further) finance, three times the level in 2019:

Had a funding need

By date of interview

Over time – row percentages

	2018	2019	2020
All SMEs	4%	3%	9%
0 employee	4%	2%	8%
1-9 employees	5%	6%	10%
10-49 employees	6%	5%	10%
50-249 employees	3%	3%	8%
Minimal external risk rating	3%	2%	5%
Low external risk rating	4%	4%	8%
Average external risk rating	3%	3%	8%
Worse than average external risk rating	5%	3%	9%
Agriculture	5%	6%	9%
Manufacturing	3%	2%	7%
Construction	3%	3%	6%
Wholesale/Retail	6%	5%	8%
Hotels & Restaurants	5%	6%	12%
Transport	4%	2%	13%
Property/Business Services etc.	4%	3%	9%
Health	4%	1%	7%
Other Community	4%	5%	10%
All SMEs excluding Permanent non-borrowers	8%	6%	14%
Current using external finance	8%	6%	19%
Not currently using external finance	2%	1%	2%

Q25 All SMEs (new Q1 2018)

Analysis by age of business also showed an increase in each age band compared to 2019. Those trading for less than 10 years were slightly more likely to report a need for finance (10-11%) compared to 7-8% of older SMEs.

All those who identified a funding need were then asked further questions about how the need arose and any actions they had taken as a result. The first question below was adjusted in Q2 2020 to include the answer 'To cope with the impact of the coronavirus pandemic' and so this table is based on answers for Q2 to Q4 2020 when this answer option was available. For consistency, all remaining tables in this section have also been presented on the same basis, based on the 10% of SMEs with a need for finance Q2-Q4 2020.

WHY FUNDING WAS REQUIRED

The first table looks at why the funding was required, with cash flow support and coping with the pandemic the top mentions. Overall, 8 in 10 SMEs with a need for finance said that it was cashflow related, boosted by the new pandemic answer, compared to a quarter needing funding for business development, with limited variation by size of SME:

Reason funding required		0	1-9	10-49	50-249
Q2-Q4 20 all SMEs who had need for funding	Total	emp	emps	emps	emps
Unweighted base:	1426	248	490	491	197
Cash flow related	81%	80%	83%	81%	72%
Working capital to help with cash flow	49%	49%	47%	49%	52%
To cope with the impact of the pandemic	33%	34%	30%	33%	19%
To cover a short term funding gap	19%	20%	17%	18%	11%
To help through trading difficulties	12%	12%	11%	17%	5%
Business development related	24%	24%	24%	22%	31%
Invest in new plant, machinery etc	11%	11%	10%	11%	12%
To fund expansion in the UK	9%	10%	7%	5%	6%
A new business opportunity	4%	4%	4%	4%	9%
To take on staff	2%	2%	3%	2%	1%
To fund new premises	1%	1%	1%	3%	3%
To fund expansion overseas	1%	1%	1%	*	2%
To take over another business	1%	1%	1%	1%	1%

Q26 All SMEs with a need for funding (new Q1 2018)

2% of SMEs said that they were approached by a bank/other funder offering them finance with a further 2% of SMEs linking their need for funding to Research and Development.

Some data is now available over time, as the table below shows. This shows how the balance tipped towards funding for cash flow purposes (81% from 49% in 2019) and away from being business development related (24% from 58% in 2019) as the pandemic took hold:

Reason funding required

By date of interview			
Over time	2018	2019	Q2-4 2020
Unweighted base:	807	739	1426
Cash flow related	42%	49%	81%
Working capital to help with cash flow	32%	37%	49%
To cope with the impact of the pandemic	-	-	33%
To cover a short term funding gap	16%	26%	19%
To help through trading difficulties	11%	12%	12%
Business development related	58%	58%	24%
To fund expansion in the UK	26%	20%	11%
Invest in new plant, machinery etc	22%	25%	9%
A new business opportunity	18%	13%	4%
To take on staff	6%	5%	2%
To fund new premises	5%	7%	1%
To fund expansion overseas	2%	3%	1%
To take over another business	1%	2%	1%

Q26 All SMEs with a need for funding (new Q1 2018)

AMOUNT OF FUNDING REQUIRED

The next table looks at how much finance was thought to be required to meet the funding need. In Q3 2019 the bands for collecting this information were narrowed to provide more granularity and extended upwards to a top band of £5 million or more. A revised table is shown below.

8% of those with a need for finance Q2-Q4 2020 could not say how much they had wanted and have been excluded from this table. As might be expected, larger SMEs with a need for funding were more likely to be looking for more than £25,000 (95% of those with 50-249 employees) than smaller SMEs were (25% of those with 0 employees):

Likely finance required

Q2-Q4 20 all SMEs who had need for funding	Total	0 emps	1-9 emps	10-49 emps	50-249 emps
Unweighted base:	1283	227	449	437	170
Less than £5000	14%	18%	4%	*	1%
£5,000 to £9,999	18%	22%	9%	3%	1%
£10,000 to £24,999	32%	35%	29%	9%	4%
£25,000 to £99,999	29%	21%	47%	51%	35%
£100,000-£999,999	7%	4%	11%	33%	45%
£1million+	*	-	*	4%	15%
£25,000 or more	36%	25%	59%	88%	95%

Q27 All SMEs with a need for funding excluding DK (new Q1 2018)

Other SMEs with a need for funding who were more likely to be seeking £25,000 or more included:

- The majority of those with a minimal or low risk rating (73% and 62% respectively), compared to around a third of those with an average rating (36%) or a worse than average risk rating (29%).
- Around a third of those trading for up to 15 years (28-37%) compared to half of those trading for more than 15 years (50%).
- There was little difference by purpose of borrowing: A third of those looking for funding for business development (35%) and a similar proportion looking for cash flow related funding (38%).

THE DECISION MAKING PROCESS

As the table below shows, almost all those with a need for funding had taken some action as a result (94%). The most common action, especially for larger SMEs, was to talk informally to the main bank (38%):

Steps taken in funding decision process

Q2-Q4 20 all SMEs who had need for funding	Total	0 emp	1-9 emps	10-49 emps	50-249 emps
Unweighted base:	1426	248	490	491	197
Had informal conversation with main bank	38%	37%	36%	54%	55%
Looked online for application advice	16%	18%	13%	11%	4%
Discussed by management in the business	14%	10%	22%	25%	18%
Sought professional advice eg accountant	12%	10%	14%	16%	10%
Considered funding within business/directors	12%	12%	12%	12%	5%
Had informal conversation with other provider	12%	12%	12%	16%	17%
Looked online for possible finance providers	12%	13%	12%	9%	2%
Prepared/reviewed plans and forecasts	10%	9%	12%	17%	6%
Spoke to other business people	8%	7%	11%	10%	2%
Looked at comparison/satisfaction sites	6%	7%	4%	3%	1%
Something else	9%	9%	8%	7%	6%
Took no action	6%	6%	4%	2%	2%

Q28 NEW All SMEs with a need for funding (new Q1 2018)

Larger SMEs with a need for funding were more likely to have spoken to their main bank or to another provider, and less likely to have considered funding from within the business, or to have looked online for funding advice or possible providers.

Overall half of these SMEs (55%) spoke to an advisor or had an informal conversation with their bank or another provider about their need for funding:

- Those with 0 or 1-9 employees were less likely to have spoken to an advisor/provider (both 54%) compared to 69% of those with 10-49 employees and 73% of those with 50-249 employees.
- There was some variation by age of SME: 56% of Starts sought advice/spoke to a provider, compared to 46-48% of those trading 2-5 or 6-9 years, 57% of those trading 10-15 years and 63% of those trading for more than 15 years.
- There was also variation by risk rating, with those with a minimal rating the most likely to have such a conversation (63%) compared to 57% with a worse than average rating, 51% with an average rating and 48% with a low rating.
- Where the SME wanted funding for cash flow, 61% had sought advice/spoken to a provider compared to 45% where the funding was for business development purposes.

Some limited analysis over time is now possible and is shown in the table below. This shows that the proportion of SMEs with a need for funding who took any action was stable across the three periods while the proportion who spoke to an advisor or had an informal conversation with their bank or another provider about their need for funding increased from 41% to 55% due to more contact with the main bank:

Initial steps taken in funding decision process	Q2-Q4		
All SMEs who had need for funding – over time	2018	2019	2020
Unweighted base:	807	739	1426
Had informal conversation with main bank	21%	18%	38%
Looked online for application advice	12%	15%	16%
Discussed by management in the business	14%	15%	14%
Sought professional advice eg accountant	19%	19%	12%
Considered funding within business/directors	10%	19%	12%
Had informal conversation with other provider	11%	18%	12%
Looked online for possible finance providers	12%	15%	12%
Prepared/reviewed plans and forecasts	11%	9%	10%
Spoke to other business people	11%	10%	8%
Looked at comparison/satisfaction sites	7%	11%	6%
Something else	25%	10%	9%
Took no action	7%	7%	6%
Spoke to advisor/ main bank/ other provider	41%	43%	55%

Q28 NEW All SMEs with a need for funding (new Q1 2018)

Those who had taken any steps to meet their funding need were then asked which of a number of options they had considered. 8 in 10 had considered making an application for finance, typically to their main bank:

Steps considered in funding decision process

Q2-Q4 20 all SMEs who took initial steps on need for funding	Total	0 emp	1-9 emps	10-49 emps	50-249 emps
Unweighted base:	1380	235	470	482	193
Making an application	81%	80%	82%	88%	92%
-Applying to main bank	67%	66%	67%	76%	78%
-Applying to finance provider not currently using	11%	11%	10%	8%	9%
-Applying to finance provider currently using	8%	7%	7%	15%	13%
-Applying to an online finance platform	6%	6%	6%	4%	3%
Finding some/all of the funding yourselves	15%	15%	16%	11%	8%
Using a broker	1%	*	3%	4%	2%
None of these	9%	10%	8%	6%	2%

Q30 All SMEs with a need for funding who took action at Q28 (new Q1 2018)

Analysis amongst SMEs with a need for funding showed that:

- Most SMEs considered making an application for finance, with larger SMEs were more likely to have done so. A minority considered self-funding, with smaller SMEs more likely to have done this.
- Consideration of an application increased slightly by risk rating, from 74% of those with a minimal risk rating to 82% of those with a worse than average risk rating.
- 79% of Starts considered making an application, in line with older SMEs (76-82%) with the exception of those trading for 6-9 years (88%).
- 84% of those already using finance considered making an application, compared to 65% not currently using finance.
- Those for whom the funding was needed for business development were slightly less likely to have considered an application (66%) than those looking for help with cash flow (86%).

Some limited analysis over time is now possible and is shown in the table below. This shows that more SMEs who took action on a need for funding considered making an application in 2020 than previously (81% Q2-Q4), driven by a higher proportion who considered applying to their main bank (67%), while fewer SMEs considered self-funding:

Steps <u>considered</u> in funding decision process: All SMEs who took initial steps on need for funding – over time	2018	2019	Q2-Q4 2020
<i>Unweighted base:</i>	781	719	1380
Making an application	67%	63%	81%
-Applying to main bank	48%	37%	67%
-Applying to finance provider not currently using	14%	19%	11%
-Applying to finance provider currently using	12%	17%	8%
-Applying to an online finance platform	10%	9%	6%
Finding some/all of the funding yourselves	22%	40%	15%
Using a broker	7%	7%	1%
None of these	19%	12%	9%

Q30 All SMEs with a need for funding who took action at Q28 (new Q1 2018)

STEPS TAKEN TO MEET FUNDING NEED

The next table looks at the steps actually taken, rather than considered, by SMEs with a funding need.

8 in 10 (80%) of all SMEs who had taken action to address a funding need went on to have a borrowing 'event' to meet that need (76% of all SMEs that originally identified a funding need). The most common borrowing 'event' was an application to the main bank, mentioned by 65% of those taking action on a need for funding and 8 in 10 of those who had any sort of borrowing event at all:

Steps taken in funding decision process

Q2-Q4 20 all SMEs who had need for funding and took initial steps	Total	0 emp	1-9 emps	10-49 emps	50-249 emps
Unweighted base:	1380	235	470	482	193
Had borrowing 'event' re need for finance	80%	78%	84%	90%	91%
<i>Applied to main bank</i>	65%	63%	68%	76%	73%
<i>Applied to finance provider currently using</i>	6%	6%	7%	12%	12%
<i>Applied to finance provider not currently using</i>	11%	12%	11%	7%	9%
<i>Applied to an online finance platform</i>	5%	5%	5%	3%	2%
Decided to fund all or part of it yourselves	12%	14%	10%	6%	6%
Decided not to take funding	5%	5%	4%	2%	*
Still deciding	5%	5%	3%	3%	4%

Q31 All SMEs with a need for funding who took action at Q28 (new Q1 2018)

Analysis showed that:

- Borrowing 'events' increased by size of SME, and SMEs with employees were more likely to have applied to their main bank.
- There was little difference in borrowing 'events' by risk rating (76-81%). 75% of Starts reported a borrowing 'event', with older SMEs more likely to have done so (85% of those trading for more than 15 years reported a borrowing event, together with 84% of those trading 2-5 years).
- Those looking for funding for business development were less likely to have had a borrowing event (64%) than those looking for cash flow funding (85%), with the former group more likely to consider putting the funds in themselves (23% v 11%).
- Those already using external finance were more likely to have had a borrowing 'event' than those not already using finance (82% v 70%).

The 80% with a borrowing ‘event’ shown above is the equivalent of 8% of all SMEs.

Some limited analysis over time is now possible. This shows that the proportion reporting a borrowing ‘event’ initially declined from 63% of those taking any action on a need for funding to 57%, due to fewer such SMEs applying to their main bank (from 40% to 29%), but then increased again to 80%, again driven by applications to the main bank (65%). The proportion of SMEs deciding to fund all or part of the need themselves initially increased (from 13% to 29%) but was back to 12% in 2020:

Steps taken in funding decision process

All SMEs who had need for funding and took initial steps – over time	2018	2019	Q2-Q4 2020
Unweighted base:	781	719	1380
Had borrowing ‘event’ re need for finance	63%	57%	80%
<i>Applied to main bank</i>	40%	29%	65%
<i>Applied to finance provider currently using</i>	12%	16%	6%
<i>Applied to finance provider not currently using</i>	14%	16%	11%
<i>Applied to an online finance platform</i>	5%	7%	5%
Decided to fund all or part of it yourselves	13%	29%	12%
Decided not to take funding	12%	11%	5%
Still deciding	16%	11%	5%
Borrowing event as % of all with original need for funding	58%	54%	76%

Q31 All SMEs with a need for funding who took action at Q28 (new Q1 2018) / All with need for funding

In 2018 and 2019 around half of all SMEs with a need for funding (not just those who took any action) who went on to have a borrowing ‘event’, but this was notably higher in Q2-Q4 2020 at 76%.

The table below summarises how consideration of different options then leads to action, for Q2-4 2020 and then how this has changed over time.

In Q2-Q4 2020, almost all of those who had considered applying for finance from somewhere (the first column) went on to have a borrowing 'event' (95%). Most of them (78%) applied to their main bank, while 24% applied to another provider, with just 4% deciding to fund some or part of the need themselves:

From consideration to action

All SMEs who had need for funding and took steps Q2-Q4 2020	Considered any appln	Considered main bank	Considered elsewhere	Considered self fund
Had borrowing 'event' re need for finance	95%	95%	98%	36%
<i>Went on to apply to main bank</i>	78%	92%	41%	32%
<i>Went on to apply elsewhere</i>	24%	11%	81%	19%
Decided to fund all or part of it yourselves	4%	4%	9%	66%
Decided not to take funding	1%	1%	*	6%
Still deciding	3%	3%	1%	4%

Q30 and 31 All SMEs with a need for funding who took action at Q28 (new Q1 2018) / All with need for funding

Most of those who considered applying specifically to their main bank (in the second column above) went on to do so (92%). Similarly, most of those who had initially considered another financial provider went on to apply to them (81%). Two thirds of those who initially considered self-funding went on to do so, while 36% of this group ending up applying for finance, typically at the main bank.

The table overleaf reports on the transition from consideration to borrowing event over time amongst those who took steps in regard to a need for finance:

- The proportion of these SMEs who considered applying for finance and then went on to do so, increased from 8 in 10 for 2018 and 2019 to almost all (95%) in Q2-4 2020. Amongst this broader pool, the proportion who went on to apply to their main bank specifically initially declined 2018 to 2019 (55% to 41%) but then increased to 78% in the current period, as the proportion who went on to apply to another provider declined to 24% (from 35% and 43%).
- In all three years the majority of those who had considered applying to their main bank went on to do so, but this was much more likely to be the case in the current period (92%) than previously (76% and 69%).
- For those who were initially considering applying to a different provider, 4 in 10 ended up applying to their main bank, up from 2 in 10 in 2018 and 2019.
- There had been an increase in the proportion self-funding in 2019 (21% of those considering applying for funds, up from 9%) but this was not maintained in Q2-4 2020 (4%) given the increased focus on applications to the main bank. Amongst those who initially considered self-funding, two thirds went on to do so (66%) unchanged from 2019.

From consideration to action over time

All SMEs who had need for funding and took steps – over time

	Considered any appln	Considered main bank	Considered elsewhere	Considered self fund
Had borrowing 'event' re need for finance				
-2018	84%	83%	84%	35%
-2019	79%	77%	78%	31%
-Q2-Q4 2020	95%	95%	98%	36%
Went on to apply to main bank				
-2018	55%	76%	18%	22%
-2019	41%	69%	18%	13%
-Q2-Q4 2020	78%	92%	41%	32%
Went on to apply elsewhere				
-2018	35%	15%	79%	23%
-2019	43%	15%	72%	21%
-Q2-Q4 2020	24%	11%	81%	19%
Decided to fund all or part of it yourselves				
-2018	9%	11%	12%	46%
-2019	21%	18%	24%	65%
-Q2-Q4 2020	4%	4%	9%	66%

Q30 and 31 All SMEs with a need for funding who took action at Q28 (new Q1 2018) / All with need for funding

Those who decided not to take finance and to put in the funds themselves or decided not to meet the funding need at all were asked further questions to determine if they had been a 'would-be seeker of finance' and this is reported in more detail in Chapter 11.

The outcome of these borrowing events to meet a funding need is explored in subsequent chapters. First the next chapter provides an overview of all the borrowing 'events' now captured on the SME Finance Monitor.