

SME FINANCE MONITOR

Q2 2022

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Shiona Davies
Director
shiona.davies@bva-bdrc.com

www.bva-bdrc.com

MANAGEMENT SUMMARY

THIS REPORT COVERS

the borrowing process from the SME's perspective, with detailed information about those who have had a need for funding and those who have been, or would have liked to have been, through the process of borrowing for their business as well as broader context information about SMEs including growth, profitability and perceived barriers to running the business.

This data was collected up to the end of June 2022, as the UK faced not only the after effects of the pandemic, but the impact of a war in Ukraine, increasing costs and the resignation of the Prime Minister. The SME Finance Monitor questionnaire has continued to adapt to new issues, with new questions added, alongside longer standing metrics such as growth use of finance.

Challenges remained for SMEs: Whilst the impact of Covid 19 has continued to wane, SMEs saw increasing costs and the current economic climate as key challenges, alongside a tighter labour market and the new trading arrangements with the EU. Whilst both business mood and expected income were better than a year ago, neither has improved much in 2022 itself.

<p>A reducing minority of SMEs saw the pandemic as a barrier</p>	<p>When the pandemic started to take effect in Q2 2020, 68% of SMEs saw it as a major barrier to their business. Over time, that proportion dropped significantly, to 15% in Q2 2022, with little variation by size except for the largest SMEs (9% a major barrier) and with slightly higher levels of concern for those in Hospitality (20%) and Transport (19%) and those using external finance (19%).</p>
<p>Instead, SMEs were more concerned about increasing costs, which are already impacting many of them</p>	<p>As the impact of the pandemic waned, the two major barriers to business in Q2 2022 were “increasing costs” (40% of SMEs) and the “current economic climate” (30% of SMEs).</p> <p>Increasing costs is a new barrier included from Q4 2021 (when 34% saw it as a major barrier). As well as seeing it as a future barrier, a similar proportion of SMEs (42% in Q2 2022) said increasing costs had <i>already</i> made a ‘significant’ impact on their business, with a further 33% saying they had been ‘somewhat’ impacted. Those in Hospitality and Agriculture were both more likely to see increased costs as a barrier (58% and 57%) and also to have already been significantly impacted (67% and 63%).</p> <p>Having increased during the pandemic (36% for 2020), the proportion seeing the economic climate as a major barrier declined to 21% in the latter half of 2021, but increased again to 30% by Q2 2022, back above pre-pandemic levels, with concern highest in Agriculture (47%) and Manufacturing (38%).</p>
<p>A stable 1 in 3 SMEs saw the new EU trading arrangements as negative for their business, citing supply chain issues and paperwork</p>	<p>When first asked in Q1 2021, 22% of SMEs reported a negative impact from the new EU trading arrangements. This increased during 2021 to 34% in Q4 and has changed little subsequently. In Q2 2022, 32% of SMEs said that the new trading arrangements with the EU had been negative for their business, while 2% said they had been positive and the majority, 66%, reported no impact.</p> <p>Those most likely to report being negatively impacted in Q2 2022 included those both importing and exporting (59%) and those in Wholesale/Retail (51%).</p> <p>In H1 2022, the main issues for those very negatively impacted were supply chain issues (71% of those very negatively impacted) followed by paper work and regulations (48%, but as much of an issue for the largest SMEs as supply chain problems)</p>

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Amongst employers, concern increased around staff retention and recruitment

In 2021, an increasing proportion of employers saw the recruitment and retention of staff as a major barrier (18% from 11% in 2020). In the first half of 2022 this increased again slightly to 21%, and to 30% of those with 10-49 employees. The sectors most likely to be facing this challenge were Health (31%), Hospitality (27%) and Construction (26%).

Far fewer anticipated a reduced income but the proportion expecting it to grow has stabilised after initial improvements post pandemic

Back in Q2 2020, 60% of SMEs thought their income over the coming months would be non-existent or down by more than 50%. This proportion has reduced steadily since (to 9% in Q2 2022).

The proportion now expecting a *higher* income than pre-pandemic increased from 3% in Q2 2020 to 19% in Q2 2021 but has been stable since (17% in Q2 2022).

Clear differences were seen by sector (31% in Agriculture expected a higher income in Q2 2022 compared to 9% in Hospitality) and by international trade (30% both importing and exporting expected a higher income in Q2 2022 compared to 16% who only traded within the UK).

And while business mood was markedly better than 2 years ago, it too has stabilised in 2022

Back in Q2 2020, just 25% of SMEs were in a 'good' mood about their business and half (49%) were in a 'poor' mood. The proportion in a good mood then increased steadily over time, to 54% in Q2 2021, but there has been little further improvement since, with 59% in a good mood in Q2 2022.

Those most likely to be in a good mood in Q2 2022 included those with 10-49 or 50-249 employees (78% and 83%), those in Construction (67%) or Manufacturing (64%), those with plans to grow (66%) and Permanent non-borrowers (67%). Those in Transport were less likely to be in a good mood (48%).

SMEs had a range of resources available to them to help them deal with current challenges: Levels of profitability and growth, whilst increasing, remained below pre-pandemic levels. Levels of innovation remained above pre-pandemic levels and SMEs remained more likely to hold £10,000 or more of credit balances, or to have seen an injection of personal funds than pre-pandemic, while use of trade credit was stable.

An increased proportion of SMEs made a profit, although still below pre-pandemic levels

Pre-pandemic, 8 in 10 SMEs typically reported making a profit in the previous 12 months. Having dropped to 60% in Q2 2021, the proportion making a profit started to increase again (65% for 2021 as a whole) and was 73% in Q2 2022. Only Agriculture was less likely to report a profit in H1 2022 than in 2021, while the sectors that had struggled most in the pandemic, Hospitality and Transport, were more likely to report a profit in H1 2022 than in 2021 but still behind their peers (55% and 61% compared to 72% overall).

Between 2018 and 2021, an increasing proportion of SMEs had seen improving profit margins as a priority (from 30% to 58%) but the proportion in H1 2022 was slightly lower (51%).

The proportion growing in the last 12 months increased again, but remained below pre-pandemic levels

29% of SMEs (excluding Starts) reported in Q2 2022 that they had grown in the previous 12 months, up from 13% in Q1 2021, but still below the more usual 4 in 10 that had grown pre-pandemic. Those most likely to report growth in H1 2022 (27% overall) included those with 10-49 employees (41%), those who both import and export (38%) and those with plans to grow again in the year ahead (40%). There was relatively little difference by sector (21%-30%) with the exception of the Health sector (17%).

As reported growth was challenged by the pandemic, the proportion reporting a decline increased from 19% in 2019 to 64% in Q1 2021. The proportion then started to reduce steadily and was 36% in Q2 2022, back in line with 2020 but still higher than the 10-14% more usually reporting a decline 2014-2017.

SMEs had used innovation to improve their business

Pre-pandemic, around 1 in 3 SMEs reported having been innovative (35% in 2019) but this was higher in 2020 (42%) and has remained so (41% in 2021 and 40% in H1 2022) and across all size bands. Innovation continued to increase by size of SME (to 72% of those with 50-249 employees in H1 2022) with limited difference by sector (36-47%) with the exception of Construction (30%). SMEs with any element of international trade were more likely to have been innovative (57-61%) than those only trading domestically (35%) and those planning to grow were also more likely to have been innovative (51%).

A stable 38% of SMEs used trade credit

In Q2 2022, 38% of SMEs were using trade credit, ranging from 33% of those with 0 employees to 7 in 10 of those with either 10-49 or 50-249 employees. This proportion has been stable since 2019 (when 37% were using trade credit) and apparently little affected by the pandemic.

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The proportion holding £10,000 or more in credit balances remained higher than pre-pandemic

Pre-pandemic the proportion of SMEs holding £10,000 or more in credit balances increased from 16% in 2012 to 23% in 2019. During 2020 and 2021 the proportion continued to increase, reaching 35% for Q4 2021 (33% for 2021 as a whole) and this position has been maintained in 2022, with 35% holding such balances in Q2. There remained a marked increase in the proportion holding such sums by size of SME, from 28% of those with 0 employees to 95% of those with 50-249 employees.

Additional analysis also showed a marked decline over time in the proportion of SMEs holding very small credit balances of less than £5,000. Overall this declined from 60% in 2019 to 45% in H1 2022, with 0 employees much the most likely to hold such small sums (50%).

33% of SMEs received an injection of personal funds, somewhat lower than in 2021 but still higher than pre-pandemic

Pre-pandemic, around a quarter of SMEs reported an injection of personal funds, but during 2020 and 2021 this proportion increased, reaching 40% in Q2 2021. Since then the proportion has fluctuated somewhat, and was 33% in Q2 2022, in line with 2020 and above typical pre-pandemic levels.

The majority of those who reported an injection of funds in Q2 2022 said it was something that 'had to' be done (22% of all SMEs), somewhat lower than the 28% in Q2 2021, but well above levels 2015-2019 when around 1 in 10 had felt they 'had to' inject funds. Since 2020 around 1 in 10 of all SMEs said that it had been a choice to inject the personal funds (11% in Q2 2022).

Two thirds of SMEs had access to one or more of these forms of additional support

67% of all SMEs had accessed one or more of trade credit, injections of personal funds or held £10k+ in credit balances. This increased by size of SME from 65% of 0 employee SMEs to 94% of those with 50-249 employees and as the size of SME changed so too did the mix of funding, with injections of personal funds playing less of a role and credit balances more of one.

Those using external finance such as loans and overdrafts were more likely to also be using these forms of funding (75%) than those who met the definition of a PNB (58%), and use was also lower amongst those only trading in the UK (65%) or with no plan to grow (62%).

Fewer SMEs were using external finance at all and the proportion using more than pre-pandemic has reduced somewhat, as have levels of concern about repayment. Fewer SMEs reported a need for funding or a borrowing event and whilst most applications were successful this was at a somewhat lower level than when government backed funding was being agreed

Use of external finance was in line with pre-pandemic levels

38% of SMEs were using external finance in Q2 2022, somewhat lower than the 45% using finance a year ago in Q2 2021, but more in line with pre-pandemic levels. The most likely to be using external finance remained those with 10-49 employees (55%) and was also higher for those in the Other Community and Manufacturing sectors, those trading internationally and those with plans to grow.

Fewer SMEs in Q2 2022 reported borrowing more than they had pre-pandemic and concerns around repayment were also somewhat lower

In the first half of 2021, 1 in 5 SMEs (21%) were using more finance than they had pre-pandemic including those borrowing for the first time and those taking on extra facilities or making more use of existing ones. This proportion then declined steadily to 14% in Q2 2022, and across all sizes of SME. Those with 1-9 or 10-49 employees remained the most likely to be using such extra finance.

In Q2 2022, the equivalent of 6% of all SMEs were concerned about repaying the finance they had (whether directly pandemic related or not), compared to 9% in Q2 2021. Of those using any finance, 16% were concerned about repayment in Q2 2022, down from 19% in Q2 2021, with concern highest amongst the smaller group where use of finance had increased compared to pre-pandemic, with 26% concerned in Q2 2022, down from a peak of 35% in Q3 2021.

Almost half of SMEs met the definition of a PNB, back to pre-pandemic levels

A steadily increasing minority of SMEs met the definition of a 'Permanent non-borrower', an SME with little apparent appetite for finance, reaching 46% in Q2 2022 from 37% in Q1 2021. This is back in line with pre-pandemic levels and once again more SMEs met the definition of a PNB than were using finance.

Attitudinally, SMEs remained self-reliant, but fewer saw issues getting finance and a stable 28% were "Ambitious risk takers"

Most SMEs, 86%, agreed that their plans were based on what they could afford, up slightly from 80% in 2019.

A declining minority thought it would be difficult for them to get finance (32%) down from 41% in 2019. This was much more of an issue for smaller SMEs (33% with 0 employees to 10% of those with 50-249 employees), as well as those in Health or the Other Community sectors (both 39%). A similar, more stable, proportion overall (30%) were happy to borrow to grow, and here agreement increased with size of SME, from 27% of those with 0 employees to 47% of those with 10-49 or 50-249 employees.

The "Ambitious risk takers" are those who agreed both that they wanted to be a bigger business and that they were prepared to take risks to succeed. Despite the challenging trading conditions of the past few years, the proportion meeting the definition has remained broadly stable, currently 28% of all SMEs, increasing by size from 27% of those with 0 employees to 44% of those with 50-249 and also higher for the Health sector (37%).

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Slightly fewer SMEs reported a need for funding in H1 2022	During the pandemic, the proportion of SMEs reporting a need for funding increased from 3% in 2019 to 12% in 2021. In the first half of 2022 the proportion was somewhat lower, 7%, with little difference by size of SME with the exception of those with 50-249 employees (2%).
Most of those with a need for funding went on to apply, typically to their main bank	As in 2020 and 2021, most of those reporting a need for funding in H1 2022 had needed cash flow support (74%) compared to 33% seeking funds for business development. Pre-pandemic in 2019, the reasons for funding were much more balanced (49% for cash flow and 58% for business development). Amongst those who took some action, 61% applied for finance and 49% applied to their main bank. Both of these are somewhat lower than in 2020-21 when around 8 in 10 applied, 6 in 10 to the main bank, as the proportion who decided to self-fund doubled from 12% in 2020 and 2021 to 28% in H1 2022.
Success rates in 2020-21 were higher than pre-pandemic, boosted by government schemes, but with signs of a change for the most recent applications	Overall application success rates across all products increased from 7 in 10 immediately pre-pandemic (74% for applications made Q1 18-Q2 19) to more than 8 in 10 when government backed schemes were first available (83% Q3 20 -Q4 21). Success rates in the current period are somewhat lower (73% Q1 21-Q2 22), and loans (71%) remained more likely to be successful than overdrafts (58%). Indicative success rates for the loan and overdraft applications made just in 2022 itself suggest that most overdraft applications this year were successful compared to a minority of loan applications. Only limited analysis is possible, but it currently appears that the size/age/ risk profile of those applying for loans may be affecting the outcome (more small, young SMEs with a poorer external risk rating).
Overall, most SMEs had been a Happy non-seeker of finance in Q2 2022	12% of SMEs reported a borrowing event in H1 2022. Very few had been a Would-be seeker of finance (2%), leaving the largest group as usual the Happy non-seekers (86%). The proportion reporting a borrowing event increased from 13% in 2019 to 20% in H1 2021. It then declined steadily over time to 12% currently. The proportion of Would-be seekers has changed very little over time, so it is the Happy non-seekers that have varied in size along with borrowing events, with HNS making up 85% of SMEs in 2019, 76% in Q1 2021 and 86% in Q2 2022.

Looking forward, there has been little change since Q4 2021 in the proportion planning to grow, or who feel the future offers more opportunities than threats. Future appetite for finance declined slightly and confidence of future success remained below current application success rates

1 in 3 SMEs felt that the future offered more opportunities than threats up from 1 in 5 in the pandemic

In Q2 2022, 31% of SMEs felt that the future offered more opportunities than threats. This was more likely to be the case for those with 50-249 employees (46%), exporters (44%) and those planning to grow (38%).

This most recent figure is higher than when this question was first asked in Q3 2020 in the midst of the pandemic when 19% felt that the future offered more opportunities than threats. The proportion then increased steadily to 36% in Q4 2021, but the Q2 2022 figure made no further improvement at 31% overall.

5 in 10 SMEs were planning an activity that could be linked to growth

In H1 2022, 22% of SMEs were planning to take action to reduce their carbon footprint and a similar proportion (23%) were planning to take on staff. Both activities were more likely amongst larger SMEs, with just over a third of those with 10-49 or 50-249 employees planning to tackle their carbon footprint and half planning to recruit more staff.

19% of all SMEs were planning to invest in plant/machinery or premises and the same proportion were looking to develop a new product or service.

Overall, 50% were planning one or more of the activities listed, increasing to 73% of those with 10-49 employees, 76% of those with 50-249 employees and 73% of those with plans to grow. This 50% planning activities is slightly lower than in H2 2021 (57%) as fewer smaller SMEs said they were planning to take action to reduce their carbon footprint.

4 in 10 SMEs were planning to grow

In Q2 2022, 41% of SMEs were planning to grow in the coming year, ranging from 37% of 0 employee SMEs to 60% of those with 10-49 employees. The Property/Business Services sector was the most likely to be planning to grow (49%) compared to 33% in Agriculture.

This is broadly in line with pre-pandemic figures pre-2018, but lower than the 52% planning to grow a year ago in Q2 2021, due primarily to fewer 0 employee SMEs planning to grow.

Pre pandemic, in both 2018 and 2019, a quarter of all SMEs and a third of those with employees, had both grown in the previous year and planned to grow in the coming year. By 2021, the proportion had dropped to 10% of SMEs and 14% of those with employees but was slightly higher in H1 2022 at 15% of SMEs and 22% of those with employees.

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9% planned to apply for finance, with increased appetite for funding for business development

The proportion planning to apply for new/renewed finance increased only slightly 2019 to 2020 (11% to 13%) and was back in line with pre-pandemic levels in 2021 (10%) and into 2022 (9% in Q2 2022).

Asked whether this future funding was wanted for cash flow purposes or for business development, in H1 2022, 71% said that it was for business development purposes, and 41% for cash flow (some gave both reasons), back in line with 2018-2019. During the pandemic, the focus switched very much to funding for cash flow, increasing from 43% of applications in 2019 to 76% in 2020, before declining again to the 41% seen in H1 2022. Meanwhile, the purpose of past applications remained very much focussed on cash flow, 74% in H1 2022.

There were fewer Future would-be seekers than during the pandemic, but they continued to see the current climate as the main barrier to application

In 2020, 21% of SMEs had been 'Future would-be seekers of finance' thinking that something would get in the way of a future application, up from 10-13% pre-pandemic. During 2021, that proportion declined from 22% in Q1 to 14% in Q4 and has been stable since (14% in Q2 2022), much closer to pre-pandemic levels.

In Q2 2022, 8 in 10 FWBS cited the current economic climate as the main barrier to a future application. This remained in contrast to past Would-be seekers, who mentioned the process (39%) and discouragement (30%) much more than the economic climate (4%).

Three quarters of SMEs expected to be a Future happy non-seeker of finance

With the increased future appetite for finance in 2020, fewer SMEs met the definition of a Happy non-seeker of finance (65%) but since then, as any appetite for finance declined, an increasing proportion met the definition (76% in Q2 2022), closer to pre-pandemic levels (78% in 2019).

SMEs remained less confident of success with a future application than current success rates might suggest

52% of all SMEs, whatever their plans, were confident of application success in Q2 2022, unchanged from 2020 or 2021 but lower than the 6 in 10 who were confident pre-pandemic.

In Q2 2022, 38% of those planning to apply for bank finance were confident of success, compared to 44% planning to apply elsewhere. Happy non-seekers of finance remained more confident of success with a hypothetical application (57%) and the Future would-be seekers were the least confident (36%).

All these success rates though remained lower than the actual success rates currently being reported.

