

SME Access to Finance Survey 2019

Office of the Chief Economic Adviser

June 2020

SMEs are vital to the Scottish economy¹



SMEs account for 99% of businesses in Scotland



SMEs account for 41% of turnover



55% of Scottish private sector employees work in an SME

SMEs' use and demand for external finance has fallen over time, with most SMEs relying on their own reserves



SMEs' use and demand for external finance has fallen over time



The overall value of borrowing by SMEs has fallen



15% reported a borrowing event in the last 12 months



85% did not seek finance and said nothing had stopped them from applying

Credit conditions had improved significantly and most SMEs were successful in obtaining all the finance applied for



Success rates were higher than pre-recession 2007



6% turned down in at least one application



4% of applications were rejected



8 in 10 received 100% of finance sought

However, groups of SMEs were still facing obstacles in accessing finance



More than 1 in 10 medium-sized firms and manufacturing firms rated finance as a critical problem



33% of rural SMEs felt bank branch closures were affecting their ability to access finance



Half of SMEs were not confident in understanding the different types of finance available

¹ Icons from www.flaticon.com

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Summary

Background

- Small and medium-sized enterprises (SMEs) play an important role in the Scottish economy and the use of external finance can support them to invest, innovate and grow. It is therefore important to understand whether the SME finance market in Scotland is working correctly, providing finance to viable firms.
- The Scottish Government commissioned its first survey of SME finances in 2007, and followed this up with further surveys in 2009, 2010 and 2012 to monitor the impacts of the financial crisis on SMEs' ability to access finance. The survey was reinstated in 2019 to assess the extent to which SMEs' financing patterns had changed at a time when the economy and financial landscape was significantly different to when the first surveys were undertaken.
- This report sets out the findings of the 2019 survey, undertaken over November 2019 - January 2020, prior to the onset of the Covid-19 Coronavirus pandemic in Scotland. It provides evidence on the experiences of SMEs in accessing finance at the time the survey was undertaken and provides a baseline for monitoring the impacts of the UK's exit from the EU and the Coronavirus pandemic.

Methodology

- 1,003 SMEs in Scotland took part in the survey via telephone from 4th November 2019 to 10th January 2020. The survey asked firms about their experiences in seeking finance both over the past three years and over the past 12 months, to provide a more recent snapshot of firms' experiences.
- As in previous years, the survey included a quota for the number of firms who had sought finance over the last 12 months to enable a robust analysis of the experiences of those firms. As a result of this oversampling, the survey results do not reflect the SME population's demand and use of finance. This report therefore draws on external sources to estimate current use and demand for finance.

Key Findings

Use of finance

- The proportion of SMEs using finance had declined from 2012, indicating an increasing preference to rely on internally generated resources – perhaps, in part, a legacy of the 2007-08 financial crisis.
- Credit cards and overdrafts continued to be the most common forms of external finance used by SMEs.
- RBS and Bank of Scotland continued to dominate the SME banking market in Scotland and rates of switching between banks remained low.
- Most SMEs used their main bank as a provider for most forms of finance, indicating a reluctance among SMEs to consider different providers.

Demand for finance

- SME demand for finance (which is, of course, closely linked to but not the same as use of finance) had also declined over time, again indicating SMEs had increasingly been relying on their own reserves.

- Different sources place different estimates on SMEs' demand for external finance; however, they show that only a minority of SMEs seek finance in a given year and that demand increases with business size.
- SMEs in the agriculture/primary industries were more likely than average to seek finance.
- Overdrafts, lease/hire purchase and credit cards continued to be the most sought after forms of finance. The amounts of finance most sought were less than £5,000 and £10,000-£49,999.
- The most common reason SMEs sought new finance was for cash flow purposes, indicating finance tended to be used more for day-to-day needs than for growth.
- Most SMEs who sought finance only considered one provider and most chose their provider because they had used them before, again indicating a reluctance amongst SMEs to consider new sources or types of providers.

Attitudes to using external finance and reasons SMEs do not seek finance

- The majority of SMEs who did not seek finance said they did not need it. Only a minority did not apply because they thought they would be turned down and this proportion had fallen over time.
- Two thirds of SMEs that did not seek finance were completely self-funded and the majority said they were unlikely to use finance in the following year.
- Three quarters said they would accept a slower growth rate that they could fund themselves rather than borrowing to grow faster, indicating a reluctance amongst SMEs to use external finance. This is, perhaps, a legacy of the financial crisis.

Supply of finance

- All supply measures showed a significant improvement in the success of SMEs in obtaining finance compared with prior years, indicating credit conditions for SMEs had vastly improved at the time of the survey. Indeed, success rates were higher than in 2007, before the financial crisis, suggesting that businesses were more credit-worthy or that lenders' balance sheets had improved.
- The majority of SMEs (87 per cent) who applied for finance were successful in obtaining all the finance they needed. The proportion of SMEs turned down in at least one of their applications, at six per cent, was a quarter of what it was at its peak in 2010. Just two per cent were turned down in each and every application.
- The majority of applications (89 per cent) made by SMEs were successful. The proportion of applications for finance that were rejected, at four per cent, was less than a fifth of what it was in 2010.
- Eight in ten SMEs (79 per cent) received all the finance they sought over the three years prior to the survey and almost all (97 per cent) received all they sought over the 12 months prior to the survey, indicating that credit conditions improved further over the year prior to the survey. The proportion that received none of the finance they sought over the 12 months prior, at less than one per cent, had fallen from over half in 2010.
- Somewhat surprisingly, medium-sized and lower-risk businesses were more likely to have experienced rejection. That said, lower-risk firms were more likely to receive the full amount of finance sought and medium-sized firms were more likely than average to receive at least some of the finance they sought.
- Rural SMEs were more likely than average to receive the full amount of finance sought, likely driven by the prevalence of the agriculture sector in rural areas, which saw the highest success rates of all the sectors.

- The proportion of SMEs reporting an increase in the cost of credit over the year prior to the survey had halved since 2012 and perceptions of ease of access to finance had improved across all finance types relative to 2012.

Abilities in applying for finance and use of external finance

- Just over half of SMEs felt confident in their understanding of the different forms of external finance available. SMEs felt more confident in their ability to put together an application from their main bank than other providers. This echoes the findings that most SMEs rely on their main bank for most of their finance needs and indicates there may be a need to improve SMEs' understanding of the range and benefits of the various financial products and providers available.
- Just over a third of SMEs sought external advice when considering or applying for finance and most relied on their accountant/financial adviser or main bank, suggesting there may be a need to encourage greater use of independent external advice.

Obstacles facing SMEs

- When considered alongside other factors, access to finance does not appear to present a pressing problem to SMEs as a whole. However, when considering finance in isolation, a quarter of SMEs considered it to be a problem rated 5 or more on a 1-10 scale, where a higher score indicates increasing severity. More than one in ten medium-sized firms and manufacturing businesses rated finance as a critical problem, reflecting their higher rejection rates and indicating there were still groups of firms that faced issues in accessing the finance they needed.
- Local bank branches were considered more important by rural and agriculture SMEs and a higher proportion of rural SMEs felt bank branch closures were affecting their ability to access finance.

Interpretation

The survey results indicate that credit conditions for SMEs had improved vastly over the past decade, with success rates higher in 2019 than pre-financial crisis levels. The majority of SMEs applying for finance were successful in obtaining all they needed. However, there were groups for which success rates were lower and who were more likely to consider access to finance a problem including, somewhat surprisingly, larger SMEs as well as manufacturing firms. In addition, rural firms had been more affected by recent bank branch closures.

Alongside this improvement on the supply side, the results also demonstrate that the use of and demand for external finance by SMEs in Scotland had fallen over time and that only a minority of SMEs sought finance. The results suggest there is a significant reluctance amongst SMEs to use external finance, with SMEs preferring to rely on their own internally generated reserves and willing to grow slower to do so. This could potentially be hindering growth at the business level and therefore in the wider Scottish economy.

The findings suggest that there may be a need to improve SMEs' understanding of the range and benefits of the various financial products and providers available and, indeed, of the significant improvements seen in application success rates over the last decade. In addition, there appears to be a need to encourage SMEs to make greater use of independent external financial advice.

1. Introduction and background

1.1 Background to the survey

The Scottish Government commissioned its first survey of SME finances in 2007², as part of a consortium of organisations across the UK, to better understand the requirements, usage and experiences of SMEs in accessing finance. The survey, undertaken prior to the onset of the 2007/08 financial crisis, provided a useful baseline against which to compare the post-crash situation. In 2009, the Scottish Government commissioned its own SME Access to Finance Survey, with follow-up surveys conducted in 2010 and 2012³, to monitor the impacts of the financial crisis on SMEs' use of and ability to access finance. The survey was then rested over 2013 – 2018. During this time, access to finance conditions for SMEs in Scotland were monitored through the Longitudinal Small Business Survey⁴.

The SME Access to Finance survey was reinstated in 2019 to assess the extent to which SMEs' financing patterns had changed at a time when the economy and financial landscape was significantly different to when the first surveys were undertaken. The survey was undertaken over November 2019 to January 2020, **prior to the outbreak of the Covid-19 Coronavirus pandemic** in Scotland.

This report sets out the findings of the 2019 survey. It provides evidence on the experiences of SMEs in accessing finance at the time the survey was undertaken and also provides a baseline for monitoring the impacts of the UK's exit from the EU in January 2020 and the onset of the global Covid-19 Coronavirus pandemic in March 2020.

Chapter 2 outlines the survey methodology while chapter 3 provides a brief overview of the state of the Scottish economy and the SME lending landscape in the UK and Scotland when the fieldwork was undertaken. Chapter 4 examines the use of finance of SMEs, considering the types and levels of finance use, drawing on both the survey results and external sources. Chapter 5 considers SMEs' demand for finance, drawing on the survey results and external sources while chapter 6 considers SMEs' attitudes to using external finance and the reasons SMEs do not seek finance. Chapter 7 outlines the survey results on the outcomes of SMEs' applications for finance, considering their experiences over both the three years and 12 months prior to the survey. Chapter 8 considers the extent to which access to finance and other issues present a problem to SMEs and the impact of recent bank branch closures. The final chapter, 9, outlines the survey results on SMEs' abilities in applying for external finance and use of external advice.

Where appropriate and possible, the report outlines differences in results by business size, sector, firm type (exporter, new start, high growth) and location and provides comparisons with previous years' survey findings.

² Centre for Business Research, August 2008: Financing UK Small and Medium-sized Enterprises: The 2007 Survey https://www.cbr.cam.ac.uk/fileadmin/user_upload/centre-for-business-research/downloads/research-projects-output/sme-finance-report-final.pdf

³ Scottish Government, SME Access to Finance Reports: [July 2019](#), [November 2009](#), [2010](#) and [2012](#).

⁴ Scottish Government, Small Business Survey Scotland Reports: [2014](#), [2015](#), [2016](#), [2017](#) and [2018](#).

1.2 The role of SMEs and access to finance in the Scottish economy

SMEs play an important role in the Scottish economy, accounting for 99 per cent of all private sector businesses and over half of private sector employment in Scotland⁵. They contribute to employment and can drive competition and innovation which in turn drive productivity, dynamism and, ultimately, growth in the economy.

The use of external finance can support SMEs to establish, invest, innovate and grow. A lack of finance can cause cash flow problems, negatively impacting business survival rates, and hold businesses back from reaching their growth potential⁶. It is therefore important to understand whether the market for SME finance in Scotland is working correctly and providing finance to viable businesses with viable propositions.

1.3 Market failures in SME finance markets⁷

Finance markets may not always deliver efficient outcomes with the result that some viable or potentially viable businesses may be refused finance, negatively impacting economic growth. This is what is referred to as 'market failure'. Market failure in the SME finance market is most frequently associated with the problem of 'information asymmetry'. This occurs when prospective borrowers have more information about their financial viability than lenders but cannot provide lenders with sufficient financial track record or tangible collateral as security. This tends to affect certain types of firms, particularly early stage, pre-revenue, innovative and high growth potential firms. These information failures may become exacerbated in uncertain economic conditions as lenders become more risk adverse. Such firms may also receive less finance than is optimal as investors only consider the private benefits of investing in these businesses whereas the wider social benefits may be greater. This is due to the potential 'spill over' effects that new and innovative businesses can deliver to other firms in the economy through innovation and knowledge transfer.

Whilst these market failures relate to the supply (lender) side, market failures can also occur on the demand (borrower) side which mean that businesses do not seek an optimal amount of external finance. This may be due to businesses failing to fully understand the benefits of using external finance, how to access the variety of external finance available, or which type might be most suited to their situation. Businesses may also lack the skills to present their propositions to provide lenders with a full understanding of their viability.

⁵ As at March 2019, there were 354,125 small and medium-sized enterprises (SMEs) operating in Scotland, providing an estimated 1.2 million jobs. SMEs accounted for 99.3% of all private sector businesses, 55.4% of private sector employment and 41.5% of private sector turnover as at March 2019. Scottish Government, *Businesses in Scotland 2019*

⁶ Department for Business, Innovation and Skills, 2012, *SME Access to External Finance* [SME Access to External Finance](#)

⁷ Much of this has been adapted from: Department for Business, Innovation and Skills, 2012, [SME Access to External Finance](#). Please refer to the report for a fuller explanation of the market failures that can affect the SME access to finance market.

2. Methodology

1,003 small and medium-sized businesses in the private sector in Scotland were interviewed for this survey. Fieldwork was undertaken via telephone by Ipsos MORI Scotland, an independent market research company, from 4 November 2019 to 10 January 2020. The data analysis and report was completed by the Office of the Chief Economic Adviser, Scottish Government.

As with all previous Scottish Government SME Access to Finance Surveys, the 2019 survey questionnaire was largely based on the UK SME Finance Survey 2007⁸. This was to allow comparisons to be made over time on a consistent basis as much as possible. However, new questions were added over time to reflect changing circumstances. The 2019 survey asked firms about their experiences in seeking finance both over the past three years and over the past 12 months. The questionnaire included the following broad sections:

- demographic questions (both business and respondent) including size of firm, type of firm (growth, exporting, new start), industrial sector and owner characteristics;
- use of finance and borrowing patterns;
- demand for finance, where firms are asked about facilities applied for over the past three years including types of credit facilities;
- an assessment of levels of supply of finance based on firm and application rejection rates and final outcomes over the past three years;
- questions relating to accessing finance over the last 12 months to assess levels of demand for new or additional borrowing, and to explore further issues such as the (perceived) cost of credit to firms; and
- questions relating to businesses' willingness to use and apply for external finance⁹.

The sample of SMEs was primarily drawn from Dun & Bradstreet¹⁰. As in the 2010 and 2012 surveys, the 2019 survey sought to achieve a target of 400 firms who had either sought new additional lending or refinanced over the last 12 months to enable a more robust analysis of the experience of those firms. Quotas were also set by business size (number of employees), sector¹¹, location (urban/rural¹²) and for new businesses. The achieved sample is shown in the table overleaf.

⁸ Centre for Business Research, August 2008: Financing UK Small and Medium-sized Enterprises: The 2007 Survey https://www.cbr.cam.ac.uk/fileadmin/user_upload/centre-for-business-research/downloads/research-projects-output/sme-finance-report-final.pdf

⁹ These questions were new for 2019.

¹⁰ This was supplemented with additional sample from other suppliers.

¹¹ As in previous surveys, the public sector and not for profit organisations were excluded.

¹² Urban/rural locations are based on the Scottish Government's Urban Rural Classification 2013-2014.

Sample breakdown by size band and sector				
	Micro (0-9)	Small (10-49)	Medium (50-249)	Total
AB Agriculture, hunting, forestry, fishing	61	8	3	72
D Manufacturing	16	28	11	55
F Construction	64	53	18	135
G Wholesale/retail	66	52	14	132
K Business activities	106	91	26	223
HINO Hotels, /restaurants; transport, storage and communication; health/social work; and other community, social and personal services)	181	155	50	386
TOTAL	494	387	122	1,003

Throughout the analysis, weighting has been applied to the data by business size, sector and location to ensure that results are representative of the overall Scottish SME population¹³. Whilst the data has also been weighted (using the survey screening data) to take account of the oversampling of businesses that sought new additional lending or refinanced over the last 12 months, the weighting applied is not representative of the overall Scottish SME population¹⁴. Therefore the survey results do not reflect the SME population's demand and use of finance. As a result, this report draws on other sources, the BVA BDRS SME Finance Monitor¹⁵ and the UK Government Department for Business, Energy and Industrial Strategy's Longitudinal Small Business Survey¹⁶, to provide a picture of SMEs' current use and demand for finance. The survey results on businesses' experiences in seeking to access finance are not affected by this.

¹³ Data from the Businesses in Scotland 2019 publication was used to derive the weightings for business size, sector and location.

¹⁴ The survey's screening data was used to derive a target weight for the number of businesses in the SME population that sought finance. However, as the businesses screened were sampled with the sector and size band targets in mind, a disproportionately larger number of bigger businesses were sampled. The screening data is therefore not fully representative of the business population as a whole. As larger businesses are more likely to borrow, the weighted survey results on the proportion of businesses seeking finance do not accurately reflect the overall SME population.

¹⁵ The BVA BDRS SME Finance Monitor Annual Report 2018 is an independent report based on a dataset of 18,002 SMEs in the UK. The Scotland sample consists of 1,520 SMEs.

¹⁶ The UK Government Longitudinal Small Business Survey 2019 is a large scale survey of 11,002 SMEs across the UK. Results are provided separately for SMEs with employees and for SMEs without employees. In Scotland, 849 SMEs with employees and 246 SMEs without employees took part in the 2019 survey.

Where possible, the report provides comparisons with the 2012 survey (the last year the survey was undertaken) and key results disaggregated by:

- business size band: micro (0 – 9 employees – includes sole traders); small (10-49 employees) and medium (50-249 employees)
- sector (six broad sectors are considered: agriculture, hunting, forestry and fishing (Standard Industrial Classifications sections A and B); manufacturing (D); construction (F); wholesale/retail (G); business activities (K); hotels/restaurants, transport, storage and communication, health/social work and other community, social and personal services (HINO))
- location (urban/rural)¹⁷
- risk rating¹⁸
- firm type:
 - high growth firms: businesses that have stated turnover growth of 20 per cent or more per year over the last three years and had ten or more employees at the start of the three year period¹⁹
 - exporters: firms that sell goods or services overseas (outwith the UK)²⁰
 - new starts: firms that were established less than two years ago.

Where comparisons are drawn between sub-groups (e.g. size band), findings are reported in terms of differences between a particular sub-group (e.g. micro firms) and the overall finding (SMEs as a whole). Due to smaller sample sizes for sub-groups, the survey's estimates may be affected by sampling errors and therefore apparent differences of a few percentage points between sub-samples may not reflect real differences in the population. Therefore, sub-group comparisons in the report are displayed only when the difference with the overall finding is statistically significant at 95 per cent confidence level²¹.

¹⁷ Urban/rural locations are based on the Scottish Government's Urban Rural Classification 2013-2014.

¹⁸ Risk rating is based on the Dun and Bradstreet (D&B) Risk Indicator which provides an overview of the level of risk D&B believe is associated with each business. It measures this level of risk between 1 and 4 where 1 is minimum risk, 2 is low risk, 3 is average risk and 4 is above average risk.

¹⁹ This definition is in line with the OECD definition for high growth firms.

²⁰ Businesses who only export to the rest of the UK are not included.

²¹ If the difference between two estimates is said to be statistically significant, it means that only in exceptional circumstances (1 in 20 times) would we expect the true difference not to be significant.

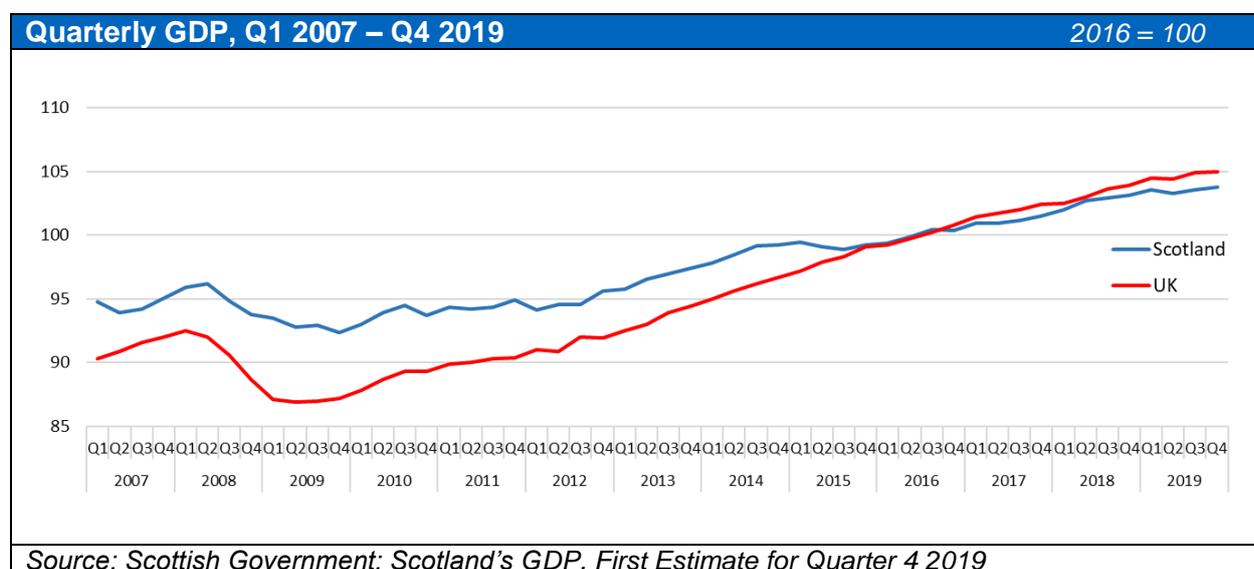
3. Macroeconomic context and recent trends in lending

3.1 Macroeconomic context

This section gives a brief overview of the state of the Scottish economy when the SME Access to Finance Survey 2019 fieldwork was undertaken. It **does not reflect the subsequent shock to the economy as a result of the global Covid-19 Coronavirus pandemic** which took hold after the survey fieldwork was completed.

The 2019 survey was conducted during November 2019-January 2020, by which time the Scottish economy and financial markets had recovered from the 2007/08 financial crisis and subsequent global recession. The survey was conducted following a period of fairly stable economic growth. However, growth was modest, reflecting weaker global growth and prolonged Brexit uncertainty from the UK's exit from the EU which was impacting business investment, sentiment and output.

During the fourth quarter of 2019, when much of the survey fieldwork was carried out, the Scottish economy grew by 0.2 per cent in real terms, following growth of 0.3 per cent in the third quarter of 2019²². Compared to the same quarter last year (2018 Q4), Scotland's GDP had grown by 0.7 per cent. The equivalent growth rates for the UK as a whole were broadly in line with Scotland²³.



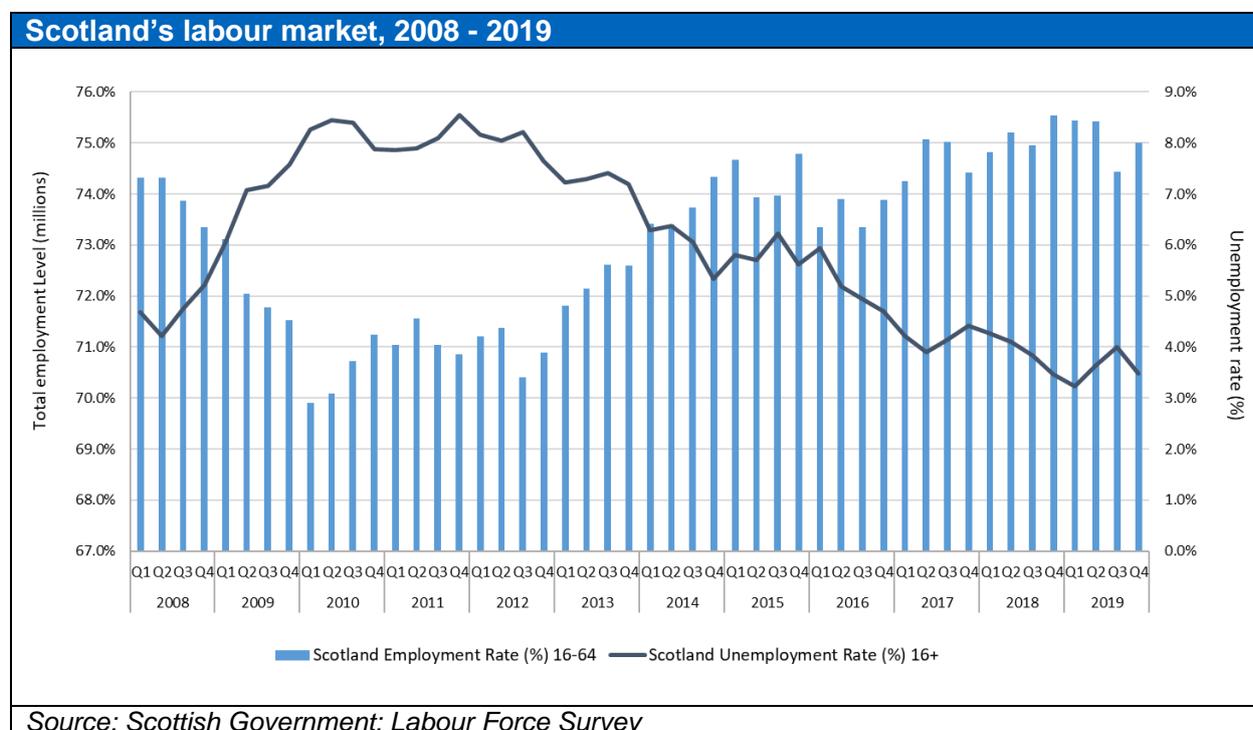
At the time the survey fieldwork was undertaken, Scotland's labour market was performing strongly compared to historic records, despite softening slightly over the year²⁴. Over the period November 2019 to January 2020, the employment rate in Scotland was 74.9 per cent, an increase of 0.4 percentage points on the previous

²² Source: Scottish Government, First Estimate of GDP: 2019 Q4

²³ The UK experienced 0.0 per cent growth in the fourth quarter of 2019 compared to the previous quarter and grew by 1.1 per cent compared to the same quarter last year.

²⁴ Source: Scotland's Labour Market: Labour Force Survey, November – January 2020

quarter and a decrease of 0.4 percentage points on the same quarter on the previous year²⁵. The unemployment rate remained low at 3.5 per cent, down 0.2 percentage points on the previous quarter and up 0.1 percentage points on the same quarter of the previous year²⁶. The labour market had improved since the last SME Access to Finance Survey in 2012, when the unemployment rate was around twice that at the time of the 2019 survey.



Evidence from the Scottish Government's National Accounts shows that business investment was weaker in 2019 relative to the prior year amid ongoing uncertainty surrounding the UK's exit from the EU and the underlying risk of a no-deal Brexit. Business Investment has increased steadily since the time of the last survey in 2012, but has slowly declined over the past three years. In 2019 Q3, business investment grew by 1.3 per cent on the previous quarter but contracted by 4.4 per cent relative to the same quarter in the previous year²⁷. Business survey intelligence²⁸ reported that business investment and confidence levels remained weak in the final quarter of 2019.

A detailed narrative on the state of the Scottish economy at this time can be found at: <https://www.gov.scot/publications/state-economy-february-2020/>

²⁵ Over the same period, the UK employment rate was 76.5 per cent. This was 0.3 percentage points up on the quarter and 0.4 percentage points up on the year.

²⁶ Over the same period, the UK unemployment rate was 3.9 per cent. This was 0.2 percentage points upon the quarter and no change on the year.

²⁷ Source: Scottish Government: Quarterly National Accounts, Q3 2019

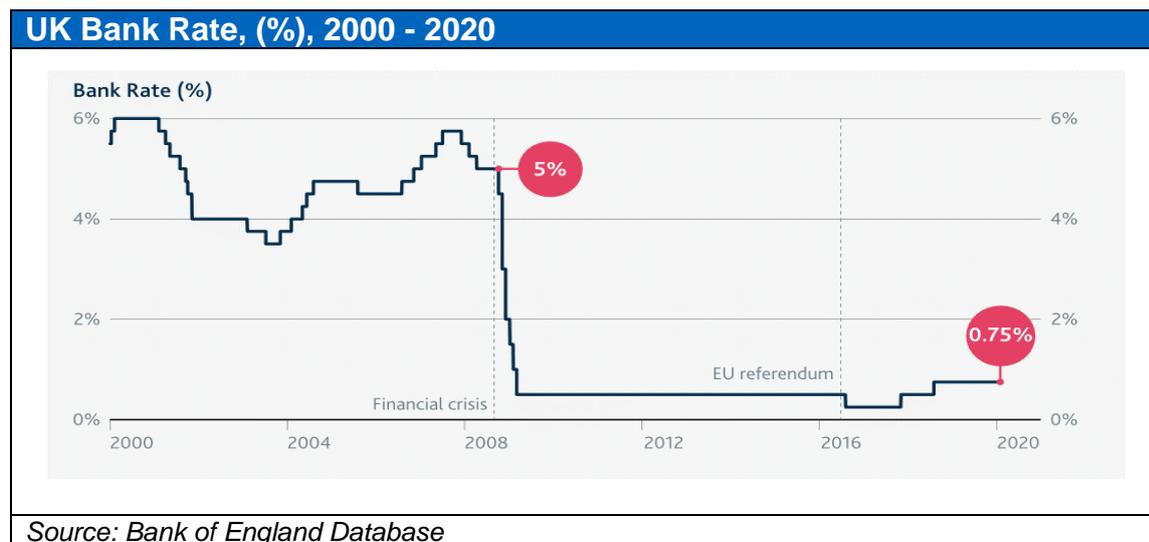
²⁸ Source: Scottish Chambers of Commerce Quarterly Economic Indicator, Q4 2019

3.2 Recent trends in lending to businesses

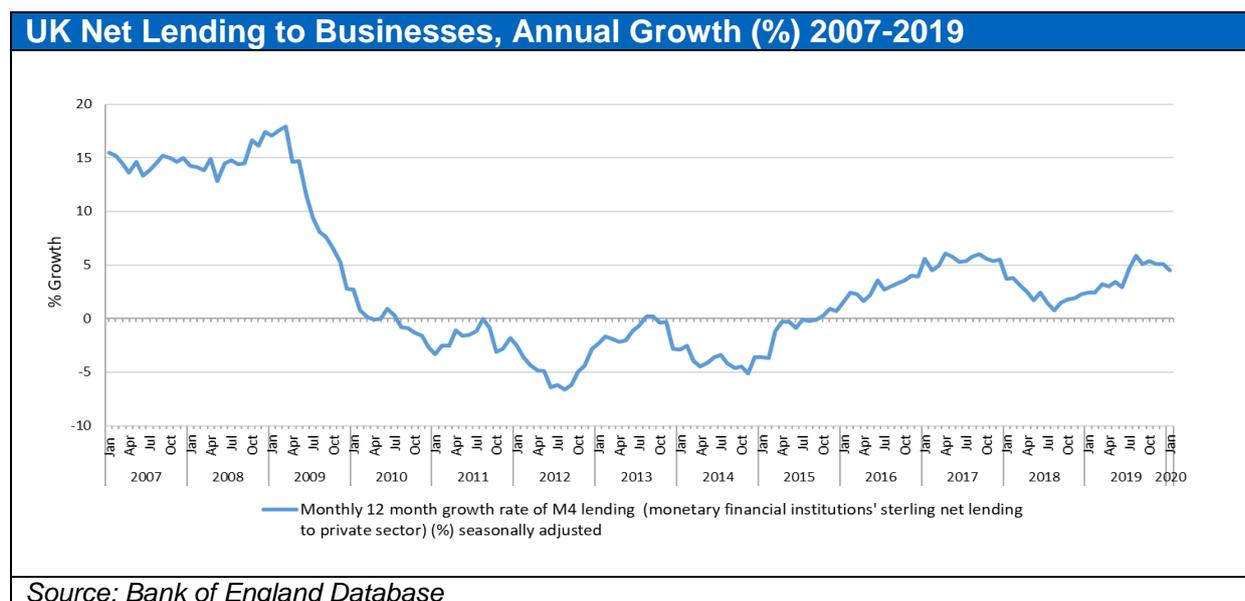
This section provides an overview of recent trends in lending to businesses in Scotland and the UK as a whole up to the period the survey fieldwork was undertaken to provide context to the survey results.

UK

The impacts of the 2007/08 financial crisis and subsequent recession still affect financial markets to this day. Over the past decade, the Bank of England has kept interest rates low to aid recovery²⁹.

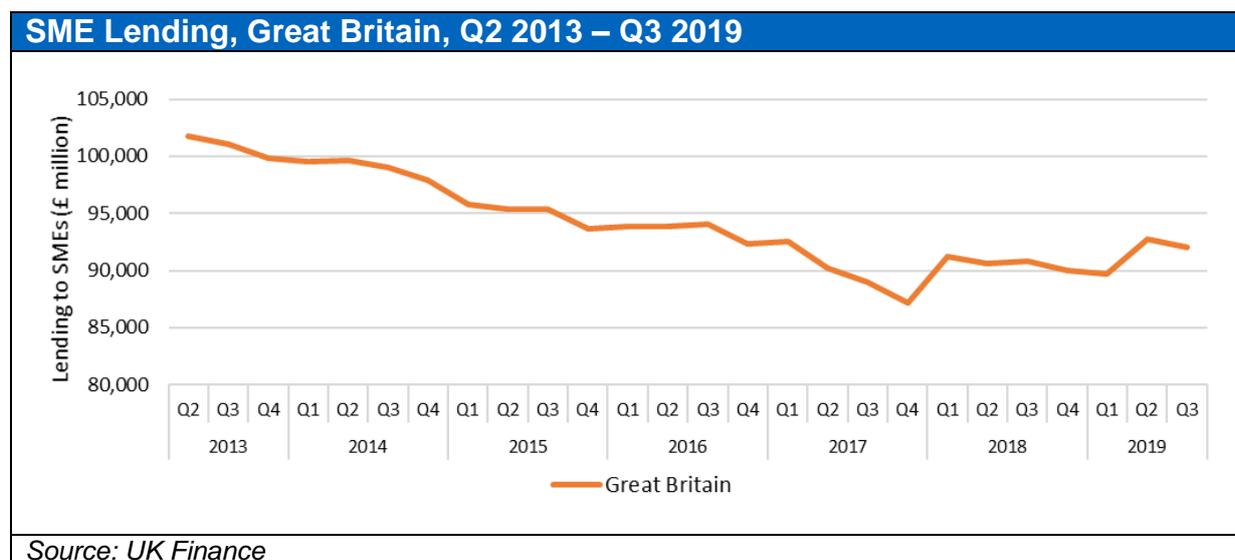


The annual growth rate of net lending to UK businesses, which saw a sharp decline at the height of the financial crisis is no longer negative, however growth has not returned to pre-recession levels.

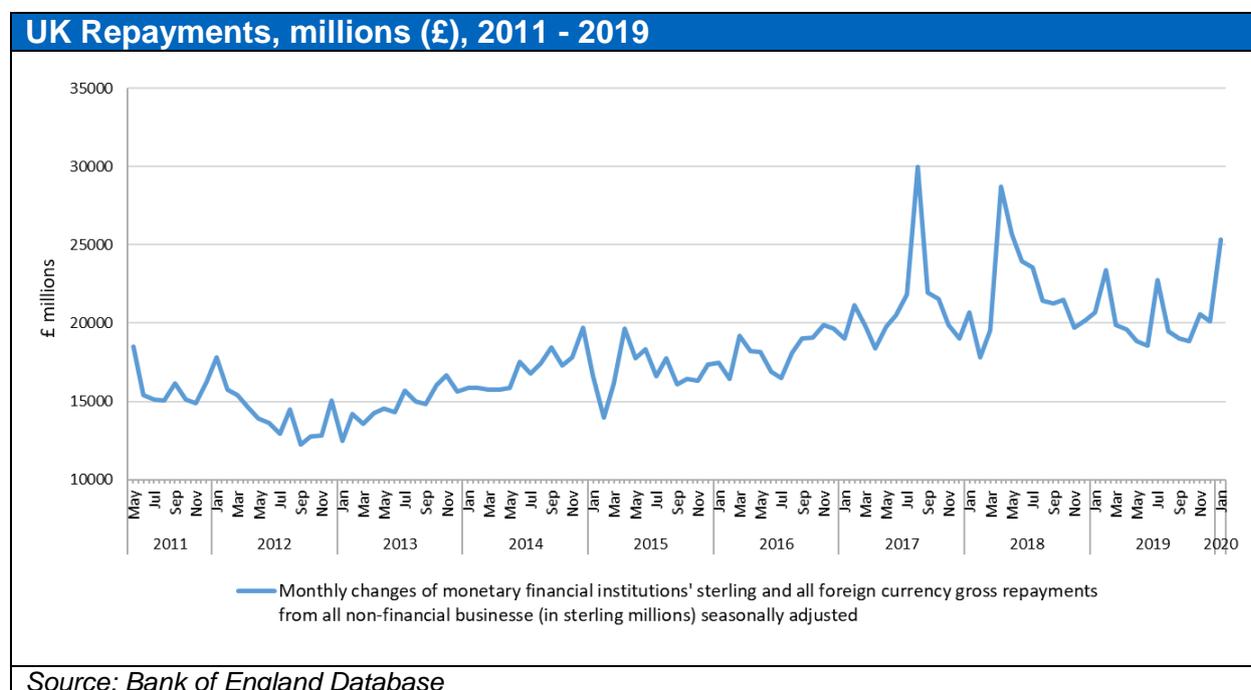


²⁹ Low interest rates encourage spending as there is less incentive to save and borrowing is cheaper.

The overall value of lending to SMEs has also declined over time.³⁰



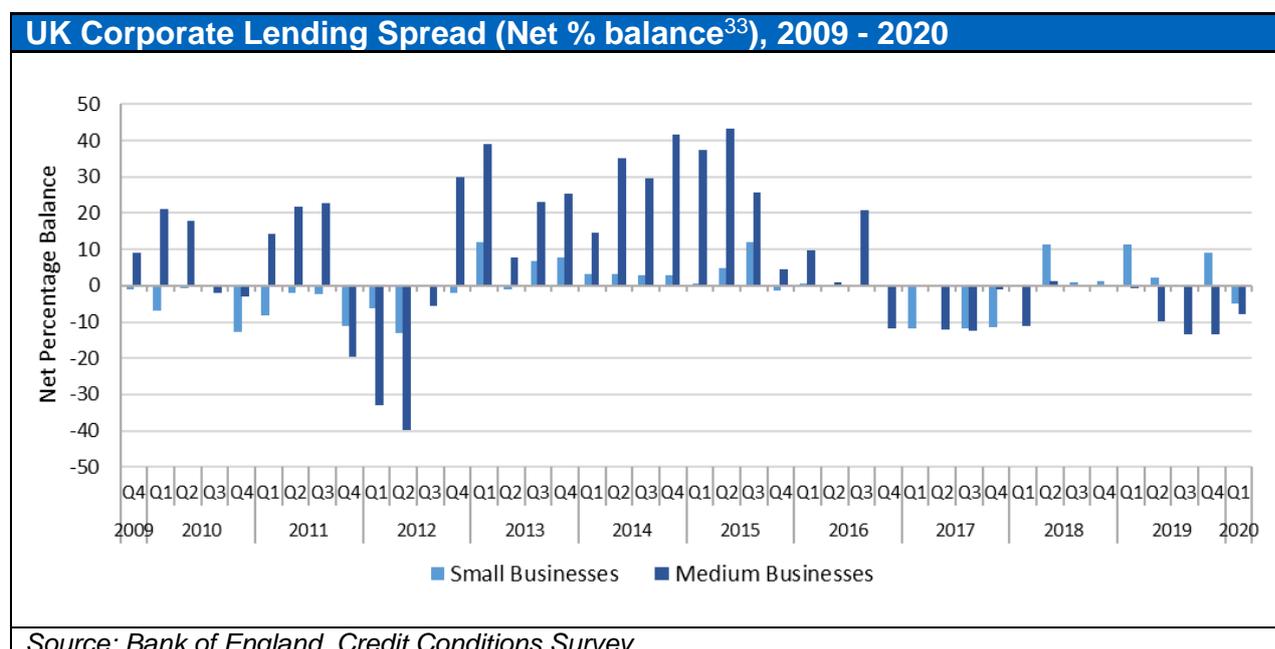
The relatively low growth in net lending and decline in overall lending levels in recent years can partly be attributed to an increase in the amount of debt that businesses are repaying. Whilst the value of repayments from UK businesses exhibits volatility, there is evidence of a gradual increase in repayments following the financial crisis. The value of repayments was higher in 2019 than in 2012, when the last SME Access to Finance Survey was conducted.



³⁰ Data not available prior to 2013 Q2.

Evidence from the Bank of England's credit conditions survey³¹ indicates that there was a fall in both the demand and supply of corporate lending over 2019 Q4. In 2020 Q1, while supply was unchanged for businesses of all sizes, demand from small businesses decreased slightly while demand from medium-sized businesses increased.

Spreads³² on lending to SMEs have narrowed (improved) since the last SME Access to Finance survey in 2012, indicating that the cost of credit to businesses has reduced. However, relative to the period 2013-16, spreads have widened (worsened) somewhat for medium-sized firms in particular. Looking specifically at the two quarters over which the survey was undertaken, spreads on lending to small firms tightened slightly in 2019 Q4 and remained broadly unchanged in 2020 Q1 while spreads had widened for medium-sized businesses over both quarters.



Scotland

Since 2012, when the last SME Access to Finance Survey was undertaken, the value of new loans to SMEs in Scotland broadly increased although it declined somewhat over 2018. Since 2015 Q2, net lending (the value of new loans less loan repayments) was, for the most part, positive for SMEs as a whole.

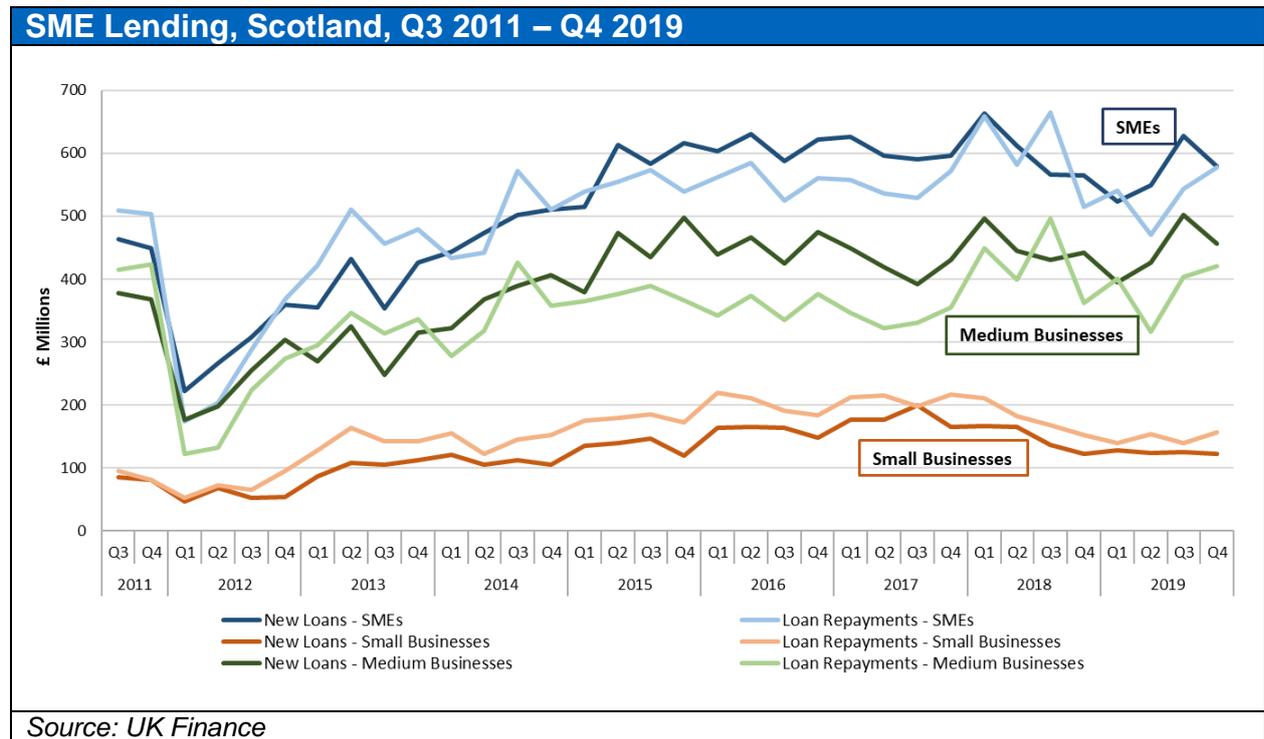
However, net lending was consistently negative for small businesses, with repayments exceeding new loans taken out. The value of new loans to small businesses in Scotland fell over 2018 and 2019. In 2019 Q4, the value of new loans

³¹ Bank of England Credit Conditions Survey 2020 Q1 (survey of bank and building society lenders)

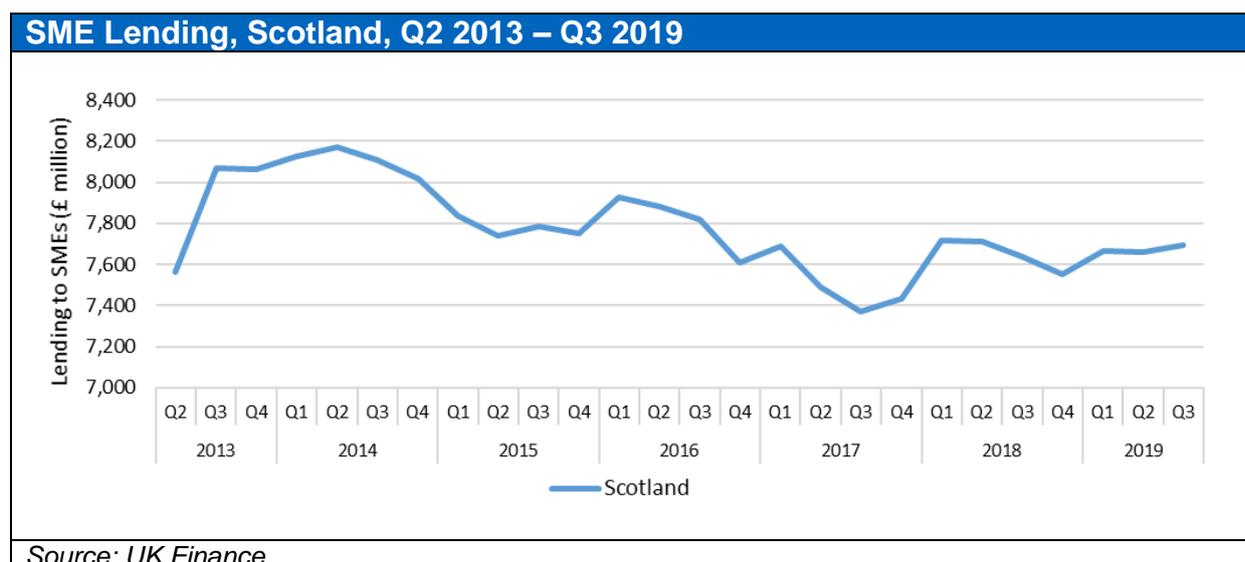
³² Credit spreads reflect the difference between the interest rates faced by businesses and the base rate set by the Bank of England.

³³ The data shows the net percentage balance of lenders reporting that spreads on loans to businesses had narrowed or widened over the quarter. A positive balance indicates spreads on loans narrowed over the quarter while a negative balance indicates spreads widened.

taken out by small businesses was down 38 per cent on 2017 Q3, when the value of new loans was at their highest over the period shown.



In terms of the overall value of lending to SMEs, while there was more fluctuation in Scotland than in GB (see figure on p12), overall lending to SMEs in Scotland declined over the period 2014-17 before picking up somewhat in 2018 and then remaining broadly stable.³⁴



³⁴ Data not available prior to 2013 Q2.

Independent market reports suggest that lower levels of lending in recent years were a result of falling demand for finance amongst SMEs rather than issues around supply³⁵. Prevailing economic conditions affected both business confidence and appetite for borrowing, while political uncertainty and Brexit negotiations added an additional level of uncertainty. SMEs appeared to be increasingly avoiding debt as a way to mitigate risk in the current climate.

The value of current account credit balances and deposit account balances of SMEs increased substantially over 2017-2019³⁶. Greater cash reserves allow businesses to self-fund more easily without the need to call on external funds. The low-interest rate environment may also have encouraged some businesses to put more personal funds into their business rather than into low-interest saving.

Evidence suggests that there has been growth in alternative lending in recent years, in particular to SMEs, with the emergence of peer-to-peer lending and crowdfunding³⁷. This has partly been driven by the decline of high street bank operations, which has allowed new suppliers to operate largely without any local market operations and work almost exclusively via phone and internet.

³⁵ [BVA-BDRC: SME Finance Monitor](#) and [Bank of England, Credit Conditions Survey, Q4 2019](#).

³⁶ [UK Finance: SME Lending and Deposits – GB 2019 Q3](#)

³⁷ [UK Finance: SME Finance in the UK: Past, Present and Future](#) and [BVA-BDRC: SME Finance Monitor](#)

4. Use of finance

Summary

- Different sources place different estimates on SMEs' use of external finance. The SME Finance Monitor suggests 39 per cent of SMEs in Scotland were using external finance in 2018 while the Small Business Survey indicates that 39 per cent for SMEs without employees and 68 per cent for SMEs with employees used finance in 2019. Both demonstrate that use of finance increased with business size.
- The proportion of SMEs using external finance has declined since 2012, indicating firms were preferring to rely on their own internally generated resources. This is perhaps a legacy of the 2007-08 recession.
- Credit cards and overdrafts continued to be the most common forms of external finance used by SMEs.
- Only six per cent of SME exporters were using export credit insurance at the time of the survey and four in ten did not know what it was, indicating a need to improve awareness of the existence and benefits of export credit insurance.
- The reasons SMEs used finance varied by finance type. Overdrafts, leasing/HP and asset based finance were mostly used to help with cash flow while loans and grants were most used to buy fixed assets / premises. Credit cards were mostly used for purchasing raw materials and expenses.
- RBS and Bank of Scotland continued to dominate the SME banking market in Scotland and rates of switching between banks remained low.
- Most SMEs tended to use their main bank as a provider for most forms of finance, indicating a reluctance amongst SMEs to consider different sources of types of providers.

This chapter examines the use of external finance by Scottish SMEs at the time the survey was undertaken. It provides an overview of the proportion of SMEs that were using external finance, and how this and their net borrowing has changed over time. It examines the types of finance SMEs used and the reasons for using finance.

4.1 Proportion of SMEs using external finance³⁸

Different sources place different estimates on the use of external finance amongst SMEs in Scotland. The SME Finance Monitor suggests 39 per cent of SMEs in Scotland were using external finance in 2018 while the Small Business Survey indicates the proportions stood at 39 per cent for SMEs without employees and 68 per cent for SMEs with employees in 2019.

SMEs' use of external finance increased with business size. The proportion of SMEs using finance has declined since 2012.

This section examines the proportion of SMEs that use external finance. The SME Access to Finance Survey results do not reflect the overall SME population's use of

³⁸ This section draws on external data sources and does not use data from the SME Access to Finance Survey.

finance due to the oversampling of SMEs that sought finance (see methodology section for more details). To estimate the proportion of SMEs currently using finance, this section therefore draws on external sources: the BVA BDRC SME Finance Monitor and the UK Government Longitudinal Small Business Survey. The BVA BDRC SME Finance Monitor data relates to 2018 whereas data from this SME Access to Finance Survey relates to the period November 2019 – January 2020.

SME Finance Monitor

The SME Finance Monitor categorises SMEs in three groupings in terms of their use of external finance: those that are using finance; those that are not using external finance but have done so in the recent past; and those who are not using finance and have not done so in the recent past. Data from the 2018 SME Finance Monitor shows that:

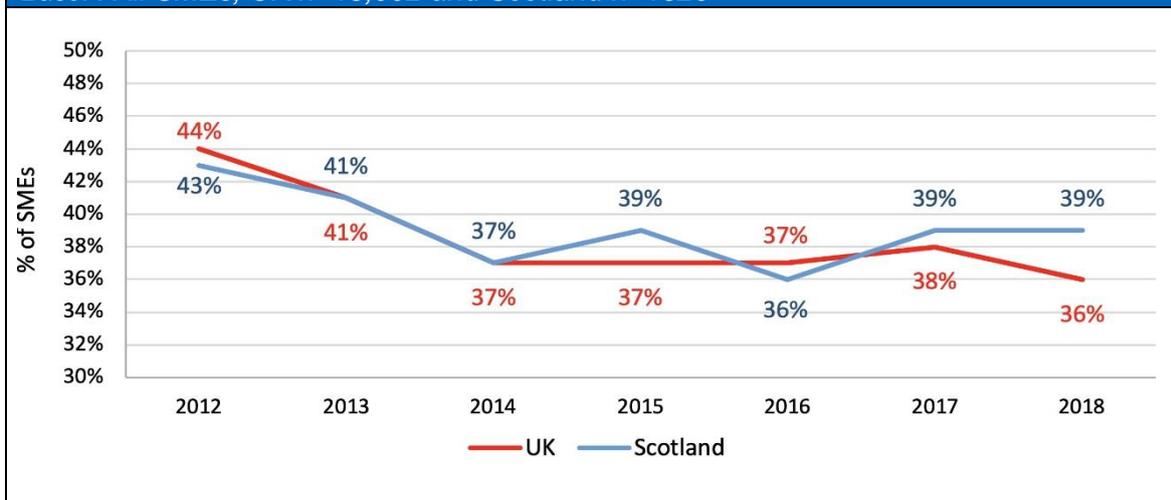
- 39 per cent of SMEs in Scotland were using at least one form of external finance at the time of the 2018 survey, a slightly proportion than in the UK as a whole (36 per cent).
- 5 per cent had used finance in the five years prior to the survey were not at the time of the survey, again a slightly higher proportion than the UK as a whole (5 per cent)
- 56 per cent had not used finance at all in the five years prior to the survey, a lower proportion that in the UK as a whole (61 per cent).

The proportion of SMEs in Scotland using finance has declined over time from 43 per cent in 2012 to 37 per cent in 2014 and has been broadly stable at 39 per cent in recent years (2017 and 2018)³⁹.

The Monitor does not provide data by business size band for Scotland however data for the UK shows that finance use increased with business size from 34 per cent of those without employees to 77 per cent of medium-sized businesses.

Figure 1: SMEs currently using any form of Finance, 2012 - 2018

Base: : All SMEs; UK n=18,002 and Scotland n=1520



Source: BVA BRDC SME Finance Monitor

³⁹ In the UK as a whole, use of finance amongst SMEs declined from 44 per cent in 2012 to 37 per cent in 2014 and has remained broadly stable since. Data is not available prior to 2012.

Small Business Survey

Data from the Small Business Survey suggests a higher proportion of SMEs in Scotland were using finance compared to the SME Finance Monitor. The survey estimates that 68 per cent of SMEs with employees in Scotland were using finance at the time of the 2019 survey (higher than the proportion in the UK as a whole at 63 per cent) while 39 per cent of SMEs without employees were using finance (lower than the proportion in the UK as a whole at 46 per cent⁴⁰). The proportion of SMEs with employees using finance has been broadly stable since 2016 while the proportion of SMEs without employees using finance decreased from 62 per cent in 2018⁴¹.

The inclusion of zero employee businesses in the SME Finance Monitor findings explains part of the difference in findings between the two sources, as zero employee businesses dominate the sample and are much less likely to use finance.

4.2 Net borrowing position

The net borrowing position of most SMEs had remained broadly stable over both the 12 months and three years prior to the survey. However, a lower proportion of SMEs increased their net borrowing over the 12 months prior to the survey than over the three years prior, indicating that SMEs may have been relying more on their own reserves than taking on new debt.

Whereas the previous section considered SMEs use of external finance at a static point in time, this section considers how their net borrowing position (level of borrowing less repayments) had changed over recent years. This section and all other sections of this chapter based on findings of the SME Access to Finance Survey.

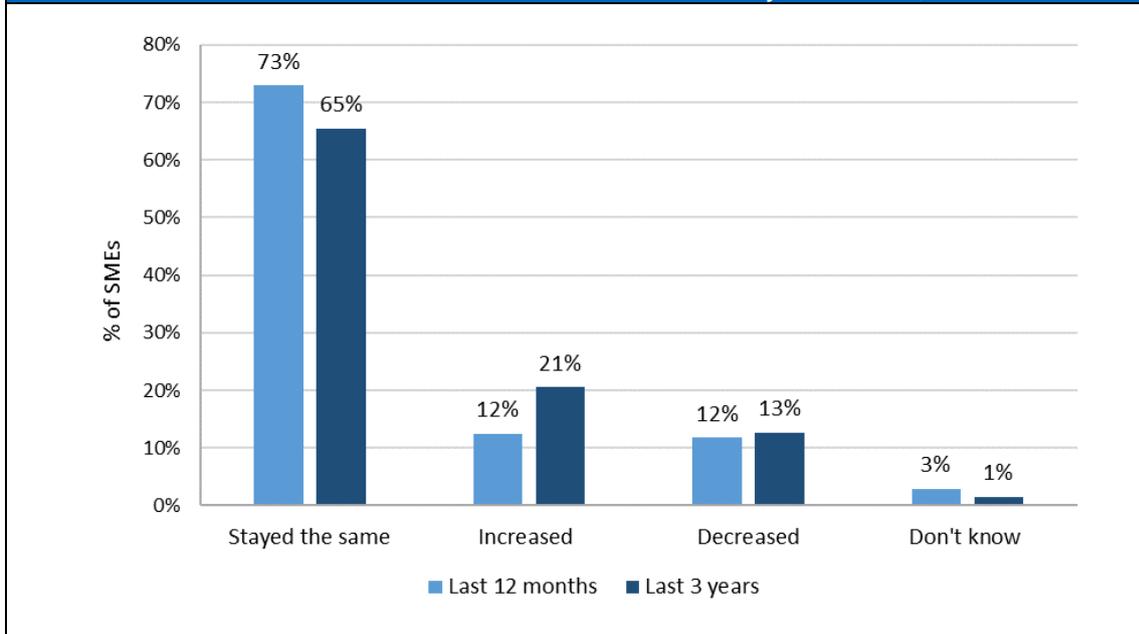
The survey asked SMEs about how their net borrowing had changed over the three years and the 12 months prior to the survey (Figure 2). The majority of SMEs reported that their net borrowing position had remained unchanged over both periods, indicating that levels of borrowing amongst those business using finance has remained broadly stable. However, a lower percentage of SMEs increased their net borrowing over the 12 months prior to the survey than over the past three years, indicating that SMEs may have been choosing to rely more on their own reserves than taken on new debt more recently.

⁴⁰ Note that the sample in Scotland for SMEs without employees is low at 246. The data for the UK as a whole may therefore be more reliable.

⁴¹ Comparable data is not available prior to 2016.

Figure 2: Change in net borrowing over the 12 months and 3 years prior to the survey

Base: All SMEs. n=1003 – minimum SMEs in business for one year or more, 947



4.3 Types of finance facilities used

Whereas the previous sections looked at SMEs' use of finance overall, this section considers the different types of finance facilities that SMEs were using at the time of the survey. It also considers SME exporters' use and understanding of export credit insurance and SMEs' use of personal current accounts.

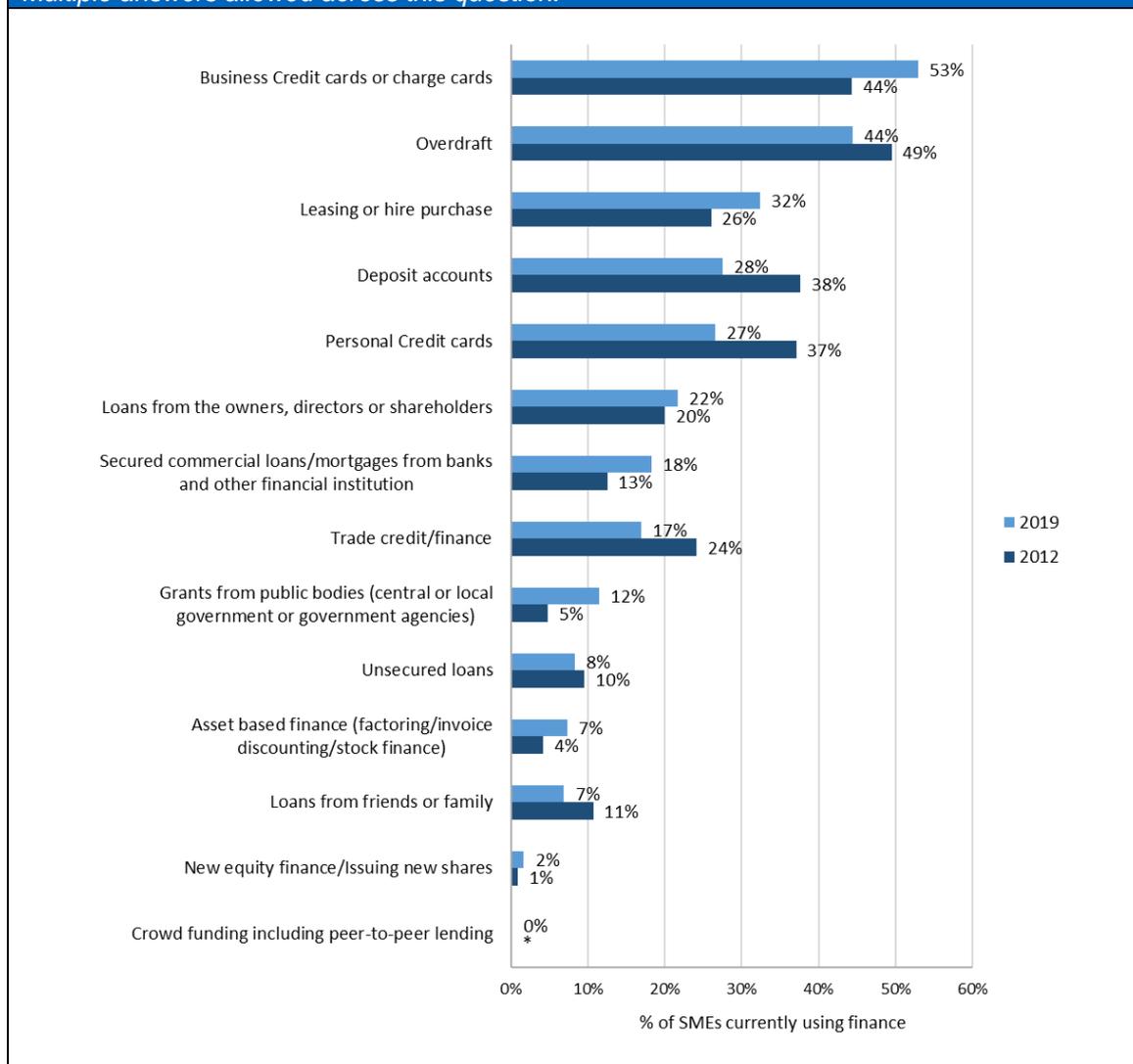
The most common types of external finance used were business credit/charge cards and overdrafts.

Of those businesses who said they were currently using external finance, the most common forms of finance used were business credit/charge cards and overdrafts (Figure 3). This is in-line with 2012, when the survey was last undertaken. Less than one per cent of businesses were using crowd funding (including peer-to-peer lending) and only 2 per cent were using equity finance.

Figure 3: Types of finance facilities used

Base: SMEs currently using finance, 2012 n=947; 2019 n=925

Multiple answers allowed across this question.



Export credit insurance

Only six per cent of SME exporters were using export credit insurance at the time of the survey and four in ten did not know what it was, indicating a need to improve awareness of the existence and benefits of export credit insurance

SME exporters⁴² were asked a number of questions about export credit insurance, which protects exporters against the risk of non-payment by foreign buyers. Only six per cent of SME exporters were using export credit insurance at the time of the survey, broadly in line with the proportion in 2012 (10 per cent)⁴³. A further 2 per cent had used it in the past but were not at the time of the survey. Over half (51 per cent) of SME exporters surveyed said they had not used export credit insurance in the past year and a further 39 per cent said that they did not know what export credit

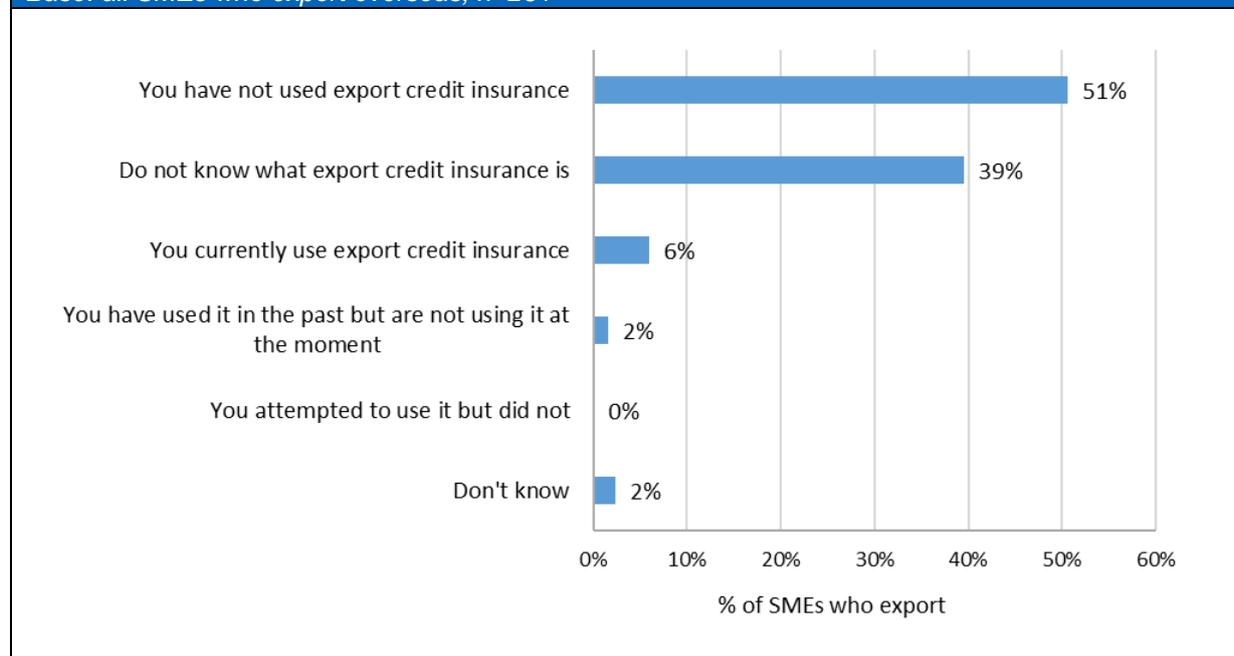
⁴² 261 SMEs sampled exported overseas.

⁴³ While it appears that the proportion dropped from 2012, the difference is not statistically significant.

insurance was⁴⁴ (Figure 4). This points to a potential need to improve SME exporters' awareness of the existence and benefits of export credit insurance.

Figure 4: Use of export credit insurance over the past year

Base: all SMEs who export overseas, n=261



SMEs with experience of export credit insurance (those either using it at the time of the survey or those who had used it in the past)⁴⁵, were asked a number of follow-up questions about their perceptions of the ease of accessing and cost of export credit insurance. Given the very low sample size (21 businesses had experience of export credit insurance), the results must be viewed with a significant degree of caution.

- In terms of ease of access of obtaining export credit insurance, around four in ten (42 per cent) felt it was just as easy to obtain relative to previous years and around four in ten (36 per cent) felt it had become harder to obtain. No SMEs reported that it had become easier to obtain⁴⁶.
- In terms of the perceived cost of export credit insurance, around four in ten (37 per cent) felt the cost was around the same as in prior years whilst around a quarter (27 per cent) felt it had become more expensive. No SMEs felt it had become less expensive⁴⁷.

⁴⁴ The option 'do not know what export credit insurance is' was not available in the 2012 questionnaire. In 2012, the proportion reporting that they had not used export credit insurance in the last year was 87 per cent, which is broadly in line with the sum of the proportions in 2019 reporting they didn't use it (51 per cent) and did not know what it was (39 per cent).

⁴⁵ 21 businesses had experience with export credit insurance.

⁴⁶ 22 per cent of SMEs with experience with export credit insurance responded 'don't know' when asked if they feel export credit insurance is harder or easier to obtain relative to previous years.

⁴⁷ 36 per cent of SMEs with experience with export credit insurance responded 'don't know' when asked if they feel export credit insurance is more or less expensive relative to previous years.

Current accounts

Only a small minority of SMEs used a personal account for business purposes

Of those SMEs that held a current account⁴⁸, the majority (94 per cent) had a business current account as their main account while 6 per cent had a personal current account.

Of those businesses that used their personal current account for their business (just 16 SMEs in the sample), almost half did so because they did not have enough business transactions to warrant a separate business account.

4.4 Reasons for using finance

The reasons SMEs used finance varied by finance type. Overdrafts, leasing/HP and asset based finance were mostly used to help with cash flow / working capital while loans and grants were primarily used to buy fixed assets / premises. Credit cards were mainly used for purchasing raw materials and expenses.

The previous section considered the extent to which SMEs used the different types of finance facilities available. This section outlines the reasons SMEs use each facility. The top three reasons cited by SMEs for using each type of finance are shown.

- **Overdrafts:** to help with cash flow (63 per cent of SMEs using overdrafts); working capital (14 per cent); for backup/safety net/just in case (13 per cent).
- **Commercial loans/mortgages or unsecured loans:** premises (33 per cent of SMEs using commercial loans/mortgages or unsecured loans); working capital (12 per cent); equipment/machinery (12 per cent).
- **Leasing/hire purchase:** to ease pressure on cash flow (69 per cent of SMEs using leasing/hire purchase); other benefits such as maintenance and replacement of faulty assets (9 per cent); didn't have enough/any security to get a loan to buy the asset (6 per cent)⁴⁹.
- **Asset based finance:** to generate working capital (77 per cent of SMEs using asset based finance)⁵⁰.
- **Personal credit cards for business purposes**⁵¹: purchase of raw materials or other supplies (32 per cent of SMEs using personal credit cards for business purposes); travel and subsistence (28 per cent); buying equipment/ vehicles (24 per cent).
- **Grant funding from public bodies:** to buy fixed assets (equipment/ machinery etc.) (29 per cent of SMEs using grant funding); to buy other assets (19 per cent); research and development for new products/services (18 per cent) and introduce new or innovative products/services (18 per cent).

⁴⁸ 91 per cent of SMEs surveyed (953 businesses) reported that they currently use a current account.

⁴⁹ A further 17 per cent cited reasons other than the options provided.

⁵⁰ A further 21 per cent stated a reason other than the options provided.

⁵¹ 190 SMEs reported that they used personal credit cards for their business.

- **Loans from family, friends or the owners, directors or shareholders of the business:** because they offered the best terms/rates (32 per cent of SMEs using loans from family, friends or owners, directors or shareholders of the business); more flexibility (25 per cent); know who I'm dealing with (13 per cent); and banks or other financial institutions would not lend at all / insufficient security (10 per cent).

4.5 Further detail on types of finance used

The previous sections have considered the extent to which and reasons why SMEs use the different forms of finance available. This section examines trends in SMEs' use of each finance type in more detail. The figures presented are as a percentage of the SMEs using each finance facility.

Overdrafts

Of those businesses who had an overdraft facility at the time of the survey⁵²:

- The most common size of overdraft facility was in the range £10,000-£49,999, cited by 41 per cent of businesses using an overdraft
- Almost of half (45 per cent) used their overdraft facility every month
- The majority (86 per cent) kept their limit the same over the past year. 8 per cent increased their limit and 6 per cent decreased it
- The majority (94 per cent) did not exceed their limit in the past 12 months

Deposit accounts

Of those SMEs that were using a deposit account at the time of the survey⁵³:

- The most common amounts held in deposit accounts were in the range £10,000-£49,999 (24 per cent), followed by less than £5,000 (18 per cent)
- 30 per cent increased the amount held in deposit accounts in the last year, 18 per cent decreased the amount held and 51 per cent kept it the same.

Commercial loans/mortgages or unsecured loans

Of those businesses that were using commercial loans/mortgages or unsecured loans at the time of the survey⁵⁴:

- The most common loan size (when the loan was originally taken out) was in the range £100,000-£499,999 (34 per cent), followed by £10,000-£49,999 (26 per cent)
- The majority (95 per cent) never failed to make repayments when due over the last year
- Over half (52 per cent) kept their level of loan/mortgage borrowing the same over the past year while almost four in ten (38 per cent) decreased it.

⁵² 382 businesses in the sample currently used an overdraft facility

⁵³ 361 businesses in the sample currently used a deposit account.

⁵⁴ 302 businesses in the sample currently used commercial loans/mortgages or unsecured loans.

Businesses currently using an overdraft and/or commercial loan or mortgage⁵⁵ were asked what type of security, if any, they provided. A third (34 per cent) provided no security while around a fifth provided a personal security (21 per cent) or charge of the business property (17 per cent). 13 per cent provided charge over their main or family home.

Personal credit cards used for business purposes

Of those businesses that were using personal credit cards for business purposes at the time of the survey:⁵⁶

- Around half charged less than £250 per month of business expenses to their personal credit card
- The majority (84 per cent) paid off in full each month the business expenses charged to personal credit cards

Business credit cards

Of those businesses that were using business credit cards at the time of the survey⁵⁷:

- The most common amount charged each month was less than £250, cited by 28 per cent
- The majority (83 per cent) paid off in full each month the business expenses charged to business credit cards.

Grants from public bodies

Of those businesses who were using grants from public bodies at the time of the survey⁵⁸:

- More than half (57 per cent) received grant funding from the Scottish Government. 18 per cent received grant funding from Scottish Enterprise and nine per cent from the European Union⁵⁹.
- The most common amounts of grant funding received were up to £5,000 (32 per cent of businesses that received grants) and £5,001-£25,000 and £25,001-£100,000, each cited by around a quarter of businesses.
- In terms of the reasons businesses sought grants, no businesses reported that it was because they could (or thought they could not) get any funding from banks or other financial institutions. Only one per cent each sought grant funding because they could not get all the funding they needed from banks or other financial institutions or because other sources of finance were too expensive or risky. The most commonly reported reason for using grant finance (cited by 44 per cent of those receiving grants) was because it was

⁵⁵ 493 businesses in the sample currently used an overdraft and/or commercial loan or mortgage.

⁵⁶ 190 businesses in the sample currently used personal credit cards for business purposes.

⁵⁷ 590 businesses in the sample currently used business credit cards.

⁵⁸ 125 businesses in the sample currently used grants from public bodies.

⁵⁹ 4 per cent of SMEs currently using grant funding from public bodies received the funding from Innovate UK; 4 per cent from their local council; 3 per cent from Creative Scotland; 3 per cent from the Construction Industry Training Board; and 1 per cent each from Highlands and Islands Enterprise, Zero Waste Scotland, Scottish Rural Development Programme and Business Gateway.

available or the business was entitled to it. The next most common reason was because they preferred to use a free form of finance (17 per cent)⁶⁰. This suggests that, at least for those surveyed, businesses were not seeking grants due to any failure of the commercial market to provide finance.

Equity finance

Only 13 of the 673 limited liability SMEs surveyed were using equity finance at the time of the survey and therefore the results below must be viewed with significant caution.

Of those limited liability SMEs that were using equity finance at the time of the survey, the most common sources of equity finance were business angel groups/syndicates and the Scottish Investment Bank (Scottish Enterprise), each cited by around a third of limited liability SMEs that were using equity finance. Most of the limited liability SMEs that were using equity finance raised £1 million or more from equity finance, cited by over three quarters of limited liability SMEs that were using equity finance.

Of those limited liability SMEs who had not applied for equity finance in the past three years and were not using it at the time of the survey⁶¹, the most commonly cited reason for not applying for equity finance were: did not need finance for the business (48 per cent); do not want to give up control of the business (44 per cent); do not need it as have finance from other sources (38 per cent); do not think it's suitable for the business (34 per cent).

Of all limited liability SMEs surveyed⁶², around one in ten (11 per cent) were planning to apply for equity finance in the next three years whilst the vast majority (85 per cent) were not⁶³.

4.6 Main provider of finance

RBS and Bank of Scotland continued to dominate the SME banking market and rates of switching between banks remained low

To gain an understanding of the concentration of the SME banking market, SMEs were asked which bank/financial institution their business primarily used (the institution with which they did the most business) and the extent to which they used other providers alongside their main bank/financial institution.

Figure 5 shows the main bank or financial institution that SMEs were using for the business in 2019. Almost two thirds of SMEs surveyed were either using Royal Bank

⁶⁰ Other reasons cited were: needed it for the business (16 per cent); cash flow (9 per cent); improve environmental impact (4 per cent); it was offered to us (3 per cent); for apprenticeship (2 per cent); needed funding for new projects/services (2 per cent).

⁶¹ 654 limited liability SMEs had not applied for equity finance in the past three years and were not currently using it.

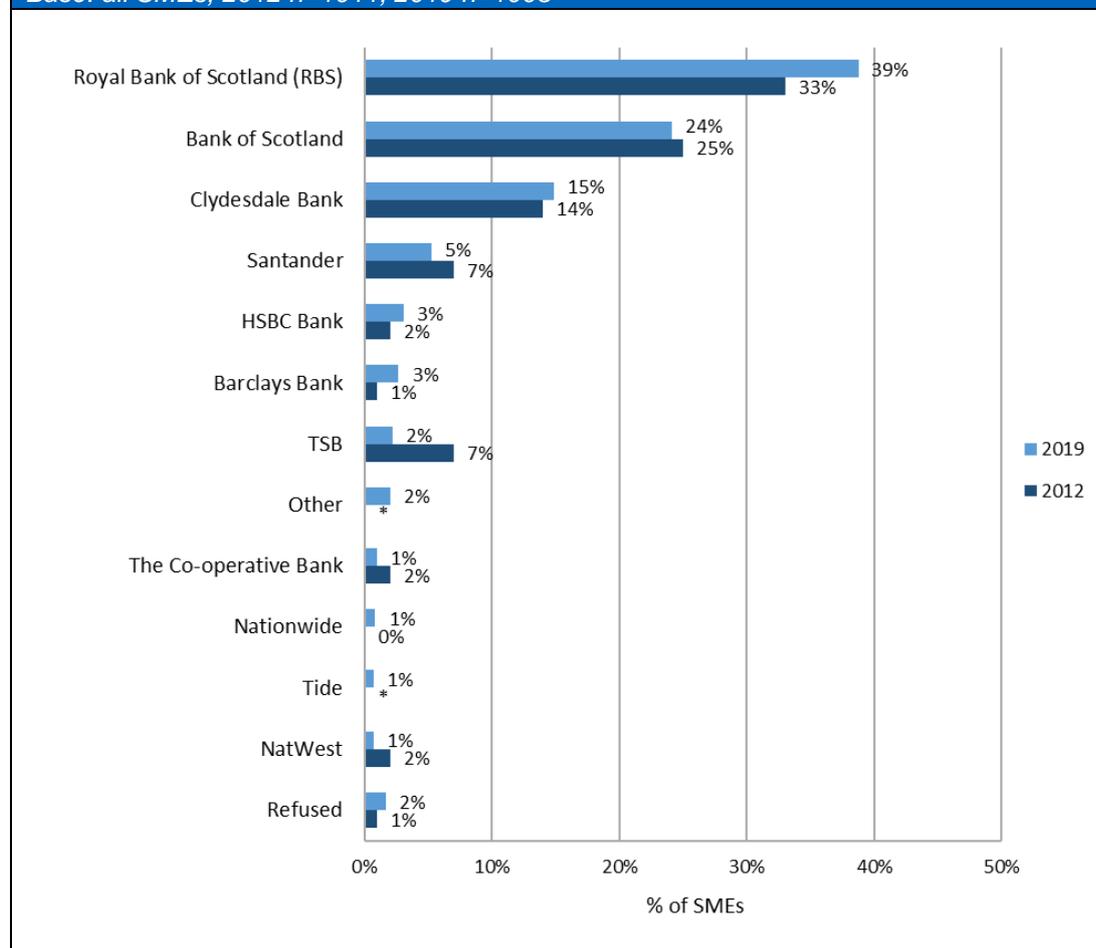
⁶² 673 limited liability SMEs were surveyed.

⁶³ 4 per cent did not know.

of Scotland (39 per cent) or Bank of Scotland (24 per cent) as their main bank⁶⁴. This was a slight increase in market concentration from 2012 when 58 per cent of SMEs cited the two banks.

Figure 5: Main bank or financial institution used by the business⁶⁵

Base: all SMEs, 2012 n=1011; 2019 n=1003



Most SMEs tend to use their main bank as a provider for most forms of finance, indicating a reluctance amongst SMEs to consider different sources or types of providers.

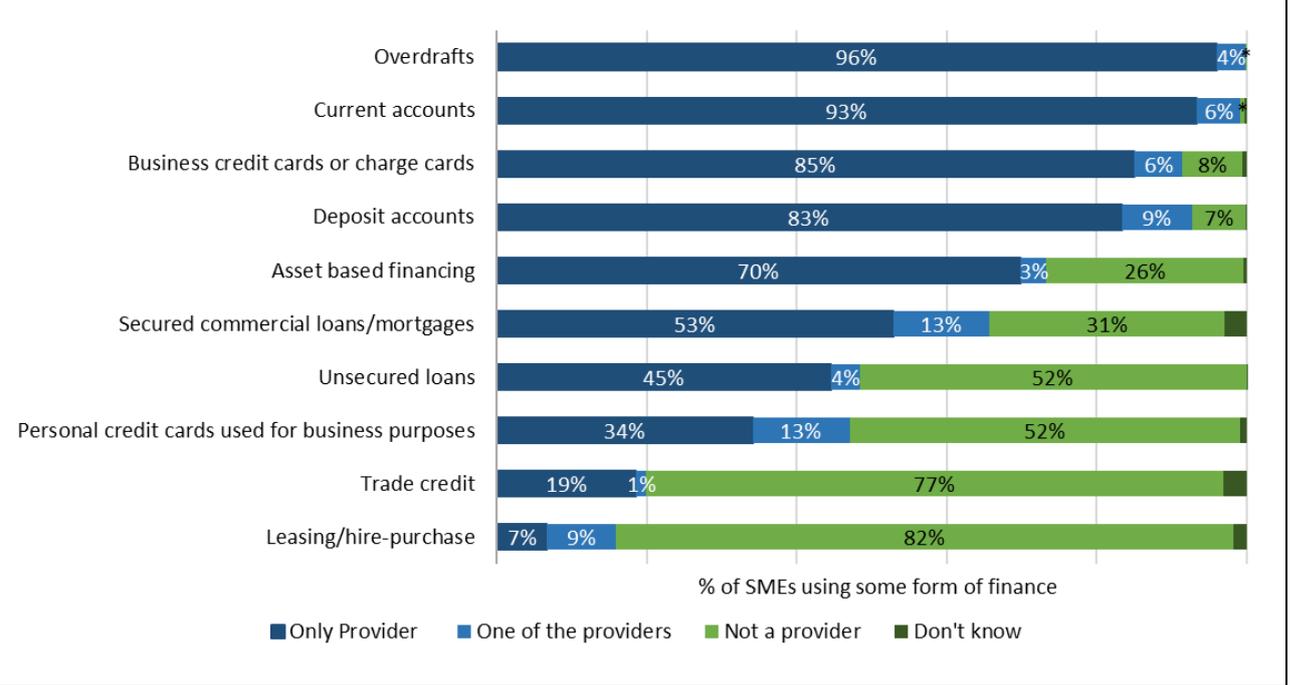
SMEs were asked if their main bank was a provider, one of the providers or not a provider of each form of finance they currently used (Figure 6). Unsurprisingly, SMEs' main bank was the only provider of external finance for the majority of SMEs using overdrafts, business credit/charge cards and deposit accounts. In contrast, SMEs' main bank was the only provider for around half of SMEs using loans.

⁶⁴ The dominance of RBS and BoS is also reflected in findings from the Small Business Survey Scotland which shows that 58 per cent of SMEs with employees in Scotland used either RBS or BoS for their current account in 2018.

⁶⁵ In the 2019 survey 'TSB' and 'Lloyds Bank' were two separate banks, however at the time of the 2012 survey they were one financial institution 'Lloyds TSB Bank PLC'. Responses for Lloyds TSB Bank PLC for 2012 are stated as TSB in Figure 5.

Figure 6: Main provider as their finance provider for each finance type

Base: SMEs using some form of finance, 980 – Base minimum: Asset based financing, 74



5. Demand for finance

Summary

- SME demand for finance had declined over time, indicating firms had increasingly been choosing to rely on their own internally generated resources. This is perhaps a legacy of the 2007-08 recession.
- Different sources place different estimates on SMEs' demand for external finance however they show that only a minority of SMEs seek finance in a given year and that demand for finance increased with business size.
- SMEs in the agriculture/primary industries were more likely than average to seek finance.
- Overdrafts, lease/hire purchase and credit cards continued to be the most sought after forms of finance. The amounts of finance most sought were less than £5,000 and £10,000-£49,999.
- The most common reason SMEs sought new finance was for cash flow purposes, indicating finance tended to be used more for day-to-day needs than for future growth.
- Most SMEs who sought finance only considered one provider and most chose their provider because they had used them before, indicating a reluctance amongst SMEs to consider new sources or types of providers.

Whereas the previous chapter outlined trends in the use of external finance at the time the survey was undertaken, this chapter examines SMEs' demand for external finance, in terms of the proportion of SMEs that sought finance in a given year. It examines the types and amounts of finance sought, the reasons why SMEs sought finance and chose their finance provider.

5.1 Proportion of SMEs seeking finance⁶⁶

Different sources place different estimates on SMEs' demand for external finance however they show that only a minority of SMEs seek finance in a given year.

SME demand for finance has declined over time, indicating firms had increasingly been choosing to rely on their own internally generated resources – perhaps a legacy of the 2007-08 recession. Demand for finance increased with business size. SMEs in agriculture/primary industries were more likely than average to seek finance.

The SME Access to Finance Survey results are not statistically representative of the overall SME population's demand for finance⁶⁷. To estimate the proportion of SMEs seeking finance, we therefore draw on two external sources, the BVA BDRC SME Finance Monitor and the UK Government Longitudinal Small Business Survey. The BVA BDRC SME Finance Monitor data relates to 2018 whereas data from this SME

⁶⁶ This section draws on external data sources and does not use data from the SME Access to Finance Survey.

⁶⁷ Please see the methodology section for further detail.

Access to Finance Survey relates to the period November 2019 – January 2020. Both sources ask SMEs about their experiences over the 12 months prior to the survey.

The figures for the proportion of firms that sought finance over the 12 months prior to the survey reported in this section are much lower than those reported in section 4.1 on the proportion of firms that were using external finance at the time of the survey in as SMEs could have applied for the finance they used at the time of the survey over several different years whereas the figure for demand represents only applications made in one year.

SME Finance Monitor

Data from the SME Finance Monitor shows that in the 12 months prior to the 2018 survey:

- four per cent of SMEs in Scotland applied for new finance or renewed existing finance
- three per cent had experienced a bank sought cancelation/renegotiation or had themselves sought a cancelation/reduction
- nine per cent had had their overdraft automatically renewed.

In total, 15 per cent of SMEs in Scotland had a 'borrowing event' (the sum of the three types of 'events' above). The proportions in Scotland reporting each type of event were broadly in line with that in the UK as a whole. Over time, the proportion of SMEs in Scotland reporting a 'borrowing event' has declined from 22 per cent in 2012 to 14 per cent in 2016 and has been broadly stable to 2018, indicating firms had instead been relying on internal sources for any finance needs.

The remaining 85 per cent of SMEs in Scotland had not had a 'borrowing event' over the 12 months prior to the 2018 survey. Of this:

- 84 per cent were 'happy non-seekers' of finance, not having had a borrowing event in the 12 months prior to the survey and saying that nothing had stopped them applying. The proportion in Scotland was broadly in line with that in the UK as a whole at 83 per cent. Between 2012 and 2016, the proportion of SMEs in Scotland meeting the definition of a 'happy non-seeker' increased from 68 per cent to 83 per cent and was broadly stable up to 2018. A similar pattern was seen in the UK as a whole.
- Just one per cent were 'would-be seekers of finance', not having had a borrowing event in the 12 months prior to the survey and saying that something had stopped them applying. Over time the proportion of 'would-be seekers' amongst SMEs in Scotland has dropped from 10 per cent in 2012 to 1 per cent in 2017 and 2018.

The reasons SMEs choose not to borrow are explored further in the next chapter.

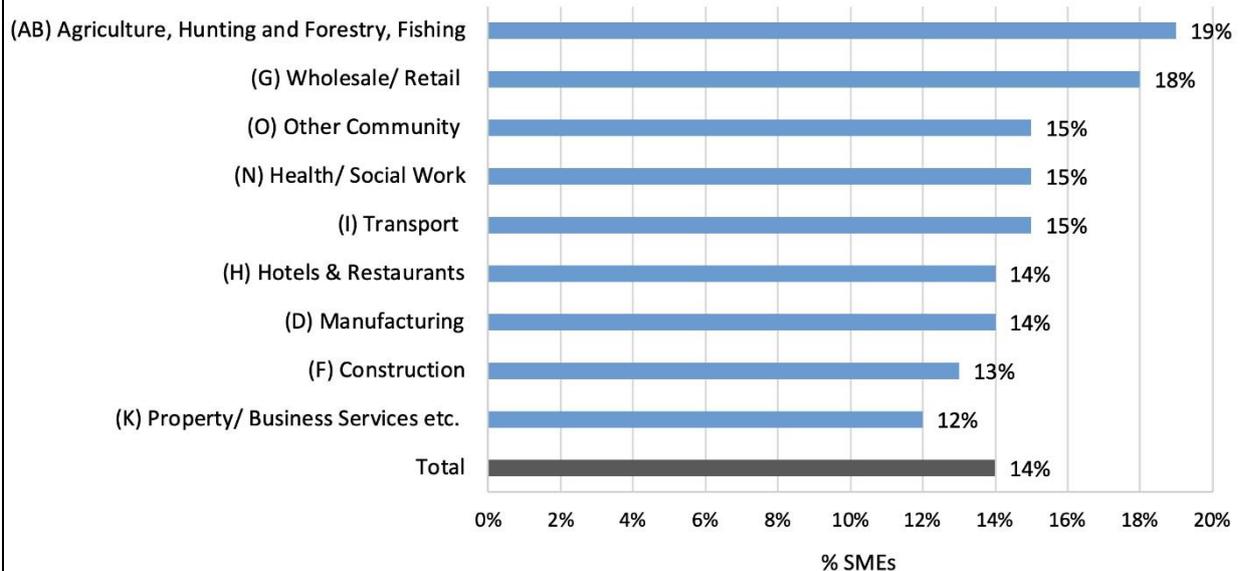
The Monitor does not provide data by business size band or sector for Scotland however data for the UK is available and is used here to provide an indication of the differences in demand for finance between business size bands and sectors.

The proportion of businesses with a ‘borrowing event’ increased with business size from 13 per cent of UK SMEs without employees to 32 per cent of medium-sized businesses⁶⁸.

SMEs in the agriculture (19 per cent) and wholesale/retail (18 per cent) sectors were more likely than average to report a borrowing event (Figure 7 below).

Figure 7: Any borrowing event in the 12 months prior to the survey, by sector, Q4 2018 (UK)

Base: all SMEs, 18,000 (base minimum: agriculture, 1200)



Source: BVA BDRC SME Finance Monitor, Q4 2018

Small Business Survey

Data from the 2019 Small Business Survey, which provides separate estimates for SMEs with and without employees, estimates that six per cent of SMEs without employees in Scotland sought external finance in the 12 months prior to the survey (compared to seven per cent in the UK as a whole), down from 16 per cent in 2012. 14 per cent of SMEs with employees had sought external finance in 2019 (compared to 12 per cent in the UK), down from 28 per cent in 2012, again indicating that firms had increasingly been choosing to rely on internal reserves for any finance needs.

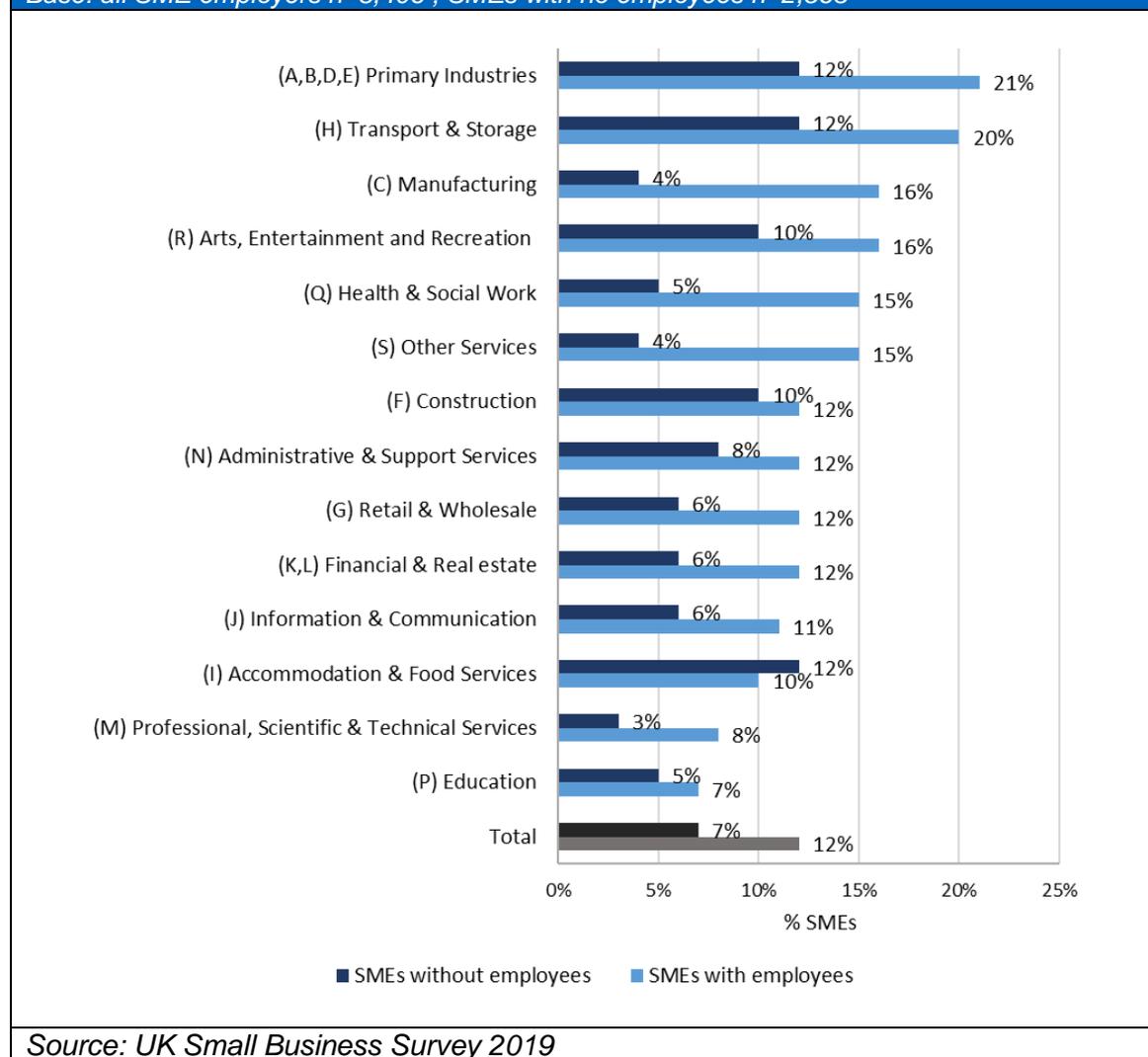
⁶⁸ Percentage of businesses with a ‘borrowing event’ in UK as a whole in 2018 by size band: 0 employees: 13 per cent; micro (1-9 employees): 17 per cent; small (10-49): 21 per cent; medium (50-249): 32 per cent. Percentage of businesses with applications for new finance or renewals in 2018 by size band: 0 employees: 3 per cent; micro (1-9 employees): 5 per cent; small (10-49): 7 per cent; medium (50-249): 4 per cent.

Medium-sized businesses with employees (23 per cent) were more likely than average to have sought external finance in 2018 when 17 per cent of SME employers sought finance (compared to 12 per cent in the UK)⁶⁹.

The Small Business Survey does not provide data by sector for Scotland however data for the UK is available and is used here to provide an indication of the differences between sectors (Figure 8 below). Of those SMEs with employees, businesses in the Primary Industries (21 per cent) and Transport & Storage (20 per cent) sectors were more likely than average to have sought finance. Of those SMEs with zero employees, businesses in the primary industries (12 per cent) were also more likely than average to have sought finance.

Figure 8: Sought external finance in the 12 months prior to the survey, 2019 (UK)

Base: all SME employers n=8,406 ; SMEs with no employees n=2,563



Source: UK Small Business Survey 2019

⁶⁹ Breakdown for business size for Scotland are not published in the UK Small Business Survey 2019. Breakdowns of the Scottish data will be provided in the separate Small Business Survey Scotland 2019 publication which was not published at the time of this report's publication. Results from the 2018 survey are therefore provided.

5.2 Types and amount of finance sought

Overdrafts were the most common type of finance sought followed by lease or hire purchase agreements and credit cards

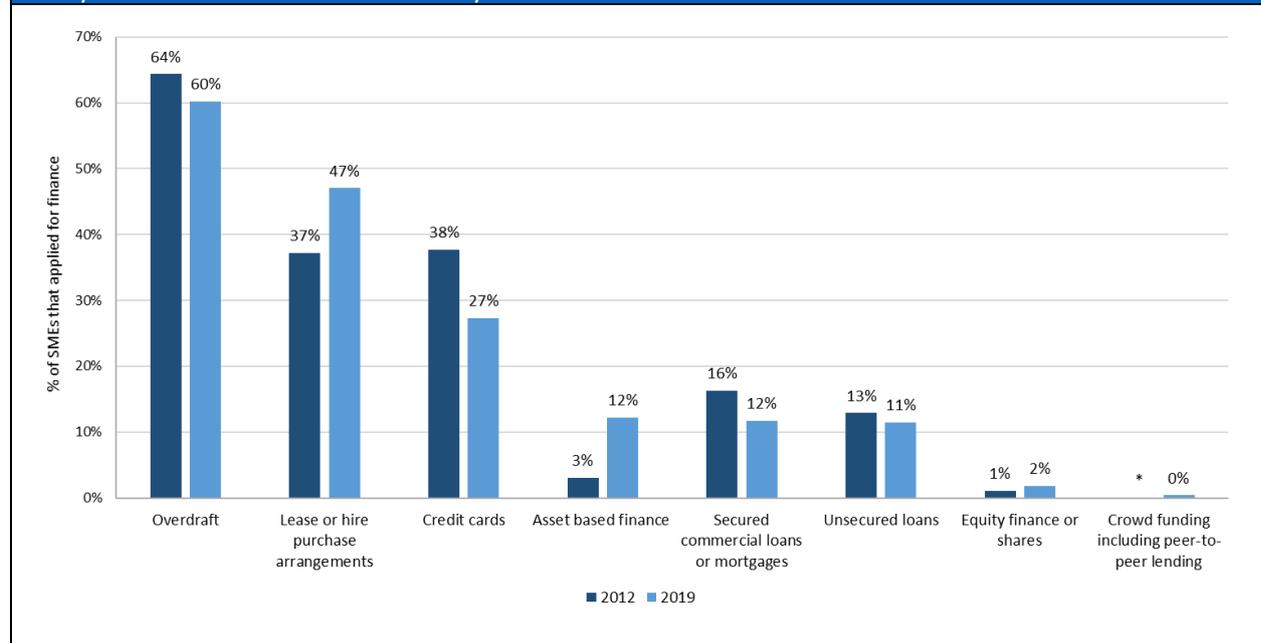
The previous section drew on external sources to examine the proportion of SMEs that sought finance and the proportion that did not. This section uses findings of the SME Access to Finance Survey to consider the types and amount of finance sought among those SMEs that had sought finance in the three years prior to the survey.

The most common types of finance sought by SMEs were overdrafts (60 per cent of SMEs who applied for any type of finance over the three years prior to the survey), lease/hire purchase agreements (47 per cent) and credit cards (27 per cent) (Figure 9). These were also the three most commonly sought finance types in 2012, when the survey was last undertaken. However, while in 2012, a similar proportion of firms sought credit cards and leasing/hire purchase, in 2019, demand for leasing/hire purchase was higher than for credit cards. In 2019, only two per cent sought equity finance⁷⁰ and less than one per cent sought crowd funding including peer-to-peer lending.

Figure 9: Type of finance applied for in the three years prior to the survey

Base: SMEs that applied for any type of finance in the three years prior to the survey, 2012 n=631; 2019 n=567

Multiple answers allowed across this question.



⁷⁰ While demand for equity finance increased from 1 per cent in 2012 to 2 per cent in 2019, this change was not statistically significant.

The amounts of finance most sought were less than £5,000 and between £10,000 and £49,999

Table 1 shows the amount of finance sought by SMEs who had applied for finance in the three years prior to the survey. The amounts of finance most sought were between £10,000 and £49,999 (26 per cent) and less than £5,000 (24 per cent). No businesses sought between £2 million and £5 million and only one per cent sought more than £5 million.

Table 1: Total new finance sought in the three years prior to the survey	
<i>Base: SMEs who applied for finance in the three years prior to the survey, 567</i>	
	Percentage of SMEs who applied for finance
Less than £5,000	24%
£5,000-£9,999	4%
£10,000-£49,999	26%
£50,000-£99,999	18%
£100,000-£499,999	13%
£500,000-£999,999	2%
£1m-£1,999,999	5%
£2-£5m	0%
£5m+	1%
Don't know/Refused	7%

5.3 Reasons for seeking finance and choosing finance provider

The most common reason SMEs sought new finance was for cash flow purposes, indicating finance tended to be used more for day-to-day needs than for future growth

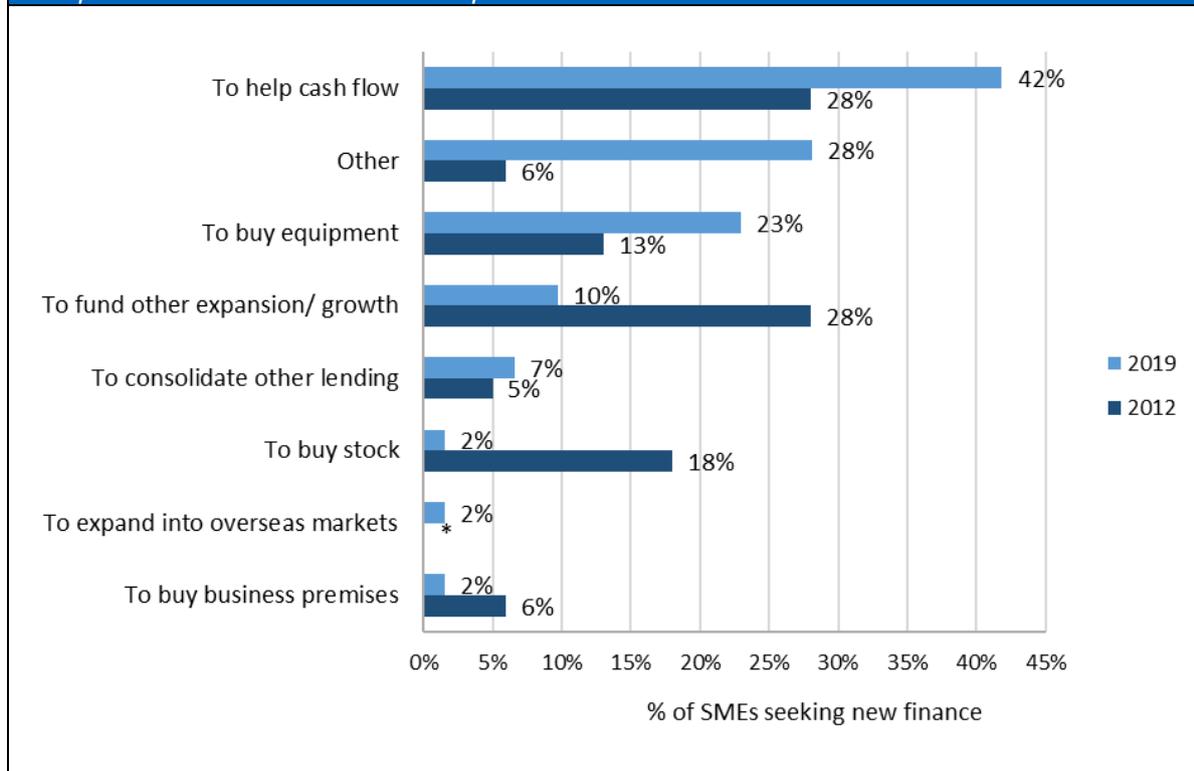
Whereas the previous section considered the types and amounts of finance SMEs had sought, this section considers the reasons they sought finance and why they chose the finance provider they most recently used.

SMEs who had sought finance in the 12 months prior to the survey⁷¹ were asked the reason they sought finance (Figure 10). The most common reason was to help with cash flow, cited by 42 per cent of SMEs who had sought new finance (up from 28 per cent in 2012). There was a significant drop in the proportion of SMEs that sought new finance to fund other expansion/ growth (10 per cent, down from 28 per cent in 2012).

⁷¹ 212 businesses sought new finance over the past 12 months.

Figure 10: Reason for seeking new finance

Base: SMEs seeking new finance in 12 months prior to survey, 2012 n=168; 2019 n=212
Multiple answers allowed across this question.

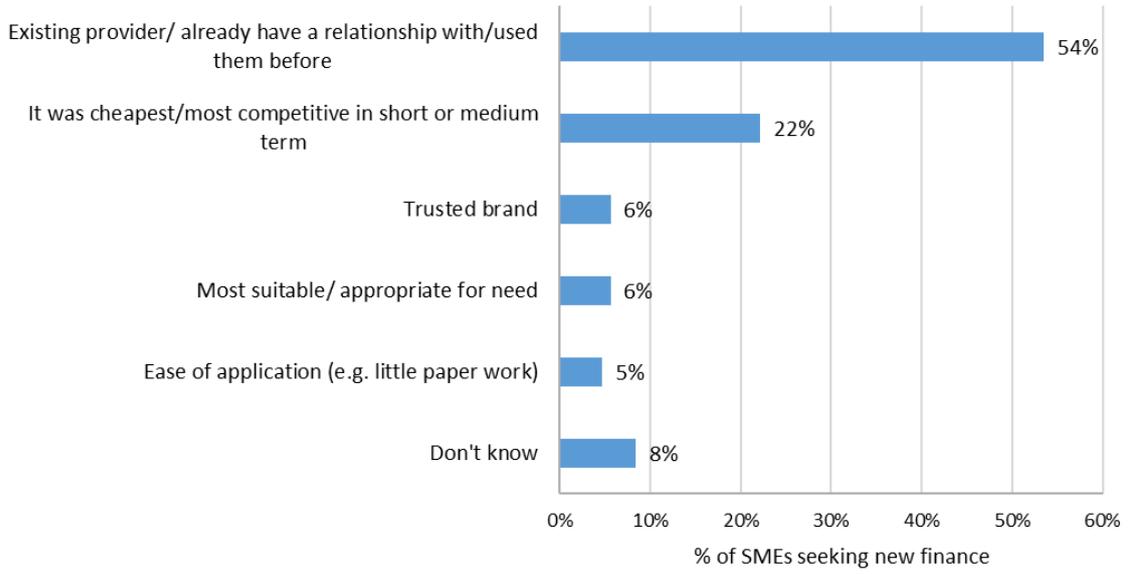


Most SMEs who sought finance only considered one provider and most chose their provider because they had used them before, indicating a reluctance amongst SMEs to consider new sources or types of providers.

Most SMEs (61 per cent) who sought new finance over the 12 months prior to the survey only considered one provider. 27 per cent considered more than one provider for new finance and 12 per cent did not know.

The most common reason SMEs chose the finance provider they last used was because they had used them before, cited by 54 per cent (Figure 11).

Figure 11: Main reason for choosing finance provider last used by the business
Base: SMEs seeking new finance in 12 months prior to survey, 212



6. Attitudes to using external finance and reasons SMEs do not seek finance

Summary

- The survey results indicate there is a reluctance amongst SMEs to use external finance.
- The majority of SMEs who did not seek finance said they did not need finance. Only a minority did not apply because they thought they would be turned down and this proportion had fallen over time.
- Two thirds of SMEs that did not seek finance were completely self-funded and the majority said they were unlikely to use finance in the following year.
- Half of all SMEs surveyed said they were happy in theory to use external finance to help grow their business, however 8 in 10 said their current plans were based entirely on what they could generate and fund themselves. Three quarters said they would accept a slower growth rate that they could fund themselves rather than borrowing to grow faster.

Section 5.1 drew on external sources to demonstrate that the majority of SMEs do not seek finance in any given year and that the proportion of non-borrowers has increased over time. This section uses findings from the SME Access to Finance Survey to look in more detail at SMEs that did not seek finance to determine the reasons why and their previous and likely future use of external finance. It also draws on a number of new questions that were added to the 2019 survey to gain a better understanding of the attitudes of all SMEs surveyed (not just those that did not seek finance) in using external finance, providing results for key sub-groups of interest.

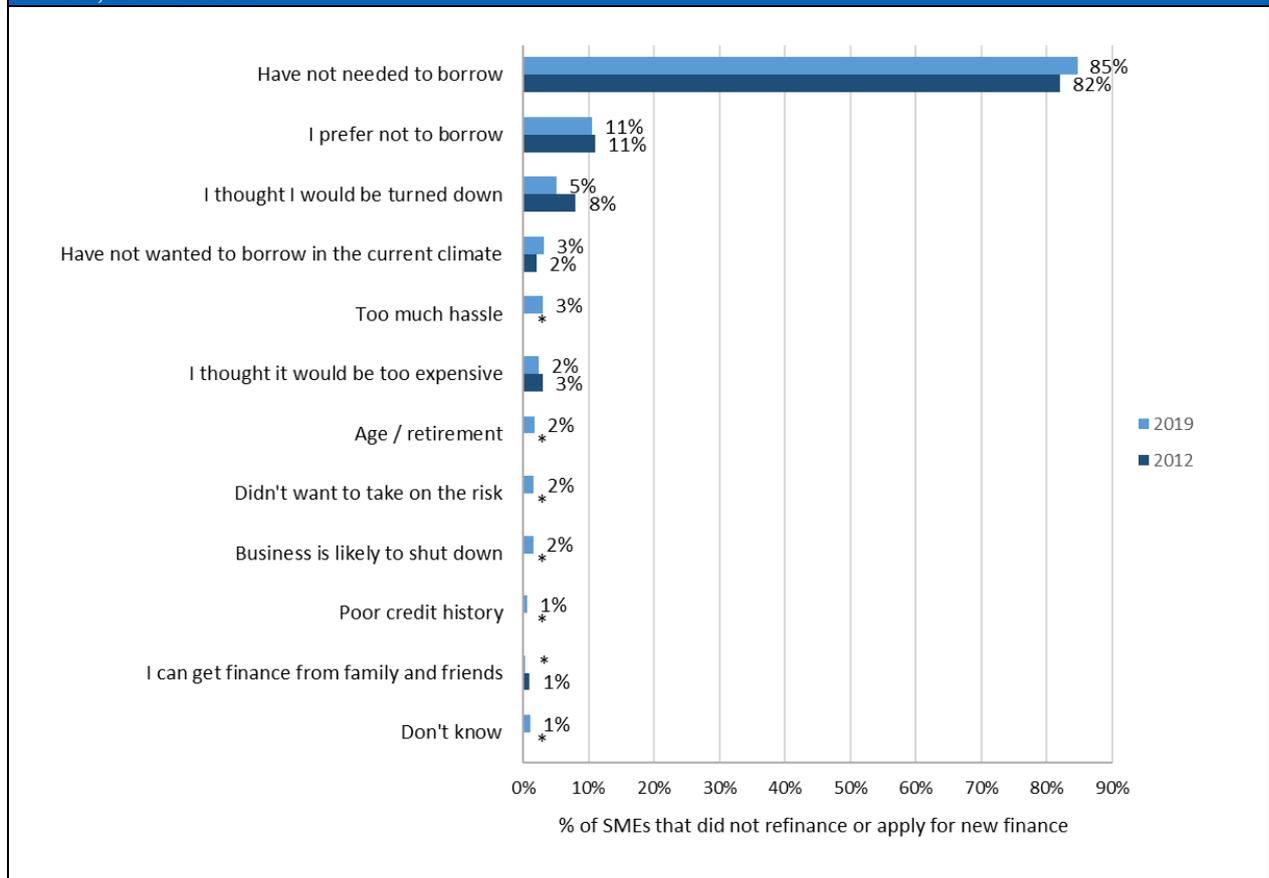
6.1 Reasons for not seeking finance

The majority of SMEs who did not seek finance said they did not need finance. A minority did not apply because they thought they would be turned down and this proportion had fallen over time.

Of those SMEs who had not applied for new finance or refinanced over the 12 months prior to the survey, the vast majority (85 per cent) said they had not sought finance because the business had not needed to borrow, broadly in line with 2012 at 82 per cent (Figure 12). Five per cent were 'indirectly discouraged' from borrowing, reporting that they did not apply because they thought they would be turned down. The proportion of businesses that were indirectly discouraged fell from eight per cent in 2012.

Figure 12: Reason for not applying for new lending or refinancing in the 12 months prior to the survey

Base: SMEs who had not refinanced or applied for new lending in 12 months prior to the survey, 2012 n=532; 2019 n=631



6.2 Previous and likely future use of finance amongst non-seekers of finance

Two thirds of SMEs that did not seek finance were completely self-funded and the majority said they were unlikely to use finance in the following year.

The previous section considered the reasons why SMEs who had not sought external finance did so. This section considers whether these SMEs had used finance in the past or are likely to use it in the future to give an indication of their attitudes to using finance over this wider time frame.

Of those SMEs that did not refinance or apply for new finance in the 12 months prior to the survey:

- most (63 per cent) said their business was completely self-funded whilst around a third (31 per cent) said they had used external finance for the business in the past
- the vast majority (85 per cent) said they were unlikely to use external finance in the 12 months following the survey with only 14 per cent said they were likely to.

6.3 Attitudes to using external finance

Half of all SMEs surveyed said they were happy in theory to use external finance to help grow their business, however 8 in 10 said their current plans were based entirely on what they could fund themselves. Three quarters said they would accept a slower growth rate that they could fund themselves rather than borrowing to grow faster, indicating there is a significant reluctance amongst SMEs to use external finance.

The previous two sections examined the subset of SMEs that had not sought finance over the 12 months prior to the survey to examine the reasons for not seeking finance and their past and likely future use of finance. This section draws on a number of new questions that were added to the 2019 survey to gain a better understanding of the attitudes of all SMEs surveyed (not just those that did not seek finance) in using external finance. The results are presented for SMEs as a whole and also, where possible, for key sub-groups of interest including size band, sector, business type (high growth/exporter/new start) and location (urban/rural).

Table 2: Willingness to use external finance: Percentage of firms agreeing to each statement

Base: All SMEs, 1003 (Micro n=494; Small n=387, Medium n=122)

	All	Micro	Small	Medium
As a business we are happy to use external finance to help the business grow and develop	49%	47%	58%	72%
Our current plans for the business are based entirely on what we can afford to fund ourselves	82%	84%	67%	81%
We will accept a slower growth rate that we fund ourselves rather than borrowing to grow faster	76%	78%	60%	63%

Half (49 per cent) of SMEs said they were **happy to use external finance to help the business grow and develop** (Table 2). Willingness to use finance appeared to increase with employee size-band, with small and medium-sized businesses more willing than SMEs as a whole to use external finance. In terms of business types, high growth firms (70 per cent) and new starts (64 per cent) were more willing than average to use external finance to grow and develop the business⁷². In terms of the sectors, firms in the construction sector (36 per cent) were less happy than average to use external finance⁷³. The results by location (urban/rural) were in line with the all-firm average.

⁷² The proportion of exporters happy to use external finance to help the business grow and develop was broadly in line with the all-firm average.

⁷³ For all other sectors, the proportion was broadly in line with the all-firm average.

8 in 10 (82 per cent) SMEs said their **current plans were based entirely on what they could afford to fund themselves**. Small firms were less likely than average to say this. Looking at the findings by sector, firms in the construction sector (91 per cent) were more likely than average to say their current plans are based on what they can fund themselves while firms in the business services sector (75 per cent) were less likely than average to say this⁷⁴. The findings by business type and location were all in line with the all-firm average.

Three quarters (76 per cent) of SMEs said they would **accept a slower growth rate that they could fund themselves rather than borrowing to grow faster**. Small and medium-sized firms were less likely to be willing to accept a slower growth rate rather than borrow. Construction firms (87 per cent) were more likely to accept a slower growth rate than borrow while business services firms (67 per cent) were less likely than average to do so⁷⁵. The findings by business type and location were all in line with the all-firm average.

⁷⁴ For all other sectors, the proportion was broadly in line with the all-firm average.

⁷⁵ For all other sectors, the proportion was broadly in line with the all-firm average.

7. Supply of finance

Summary

- All supply measures showed a significant improvement in the success of SMEs in obtaining finance compared with prior years, indicating credit conditions for SMEs had vastly improved at the time of the survey. Indeed, success rates were higher than pre-financial crisis 2007, suggesting that businesses were more credit-worthy or that lenders' balance sheets had improved.
- The majority of SMEs (87 per cent) who applied for finance were successful in obtaining all the finance they needed. The proportion of SMEs turned down in at least one of their applications, at six per cent, was a quarter of what it was at its peak in 2010. Just two per cent were turned down in each and every application.
- The majority of applications (89 per cent) made by SMEs were successful. The proportion of applications for finance that were rejected, at four per cent, was less than a fifth of what it was in 2010.
- Eight in ten SMEs (79 per cent) received all the finance they sought over the three years prior to the survey and almost all (97 per cent) received all they sought over the 12 months prior to the survey, indicating credit conditions improved further over the year prior to the survey. The proportion that received none of the finance they sought over the 12 months prior, at less than one per cent, had fallen from over half in 2010.
- Somewhat surprisingly, medium-sized and lower-risk businesses were more likely to have experienced rejection. However, lower-risk firms were more likely to receive the full amount of finance sought and medium-sized firms were more likely than average to receive at least some of the finance they sought.
- Rural SMEs were more likely than average to receive the full amount of finance sought, likely driven by the prevalence of the agriculture sector in rural areas, which saw the highest success rates of all the sectors.
- The proportion of SMEs reporting an increase in the cost of credit over the year prior to the survey had halved since 2012 and perceptions of ease of access to finance had improved across all finance types relative to 2012.

While chapter five considered SMEs' demand for finance, this chapter considers the supply side, in terms of the extent to which SMEs were able or unable to obtain the finance they sought both over the three years prior to the survey and, to provide a more recent snapshot, over the 12 months prior to the survey. It examines supply based on four measures, each of which provides different insights as outlined below:

(1) Percentage of firms turned down outright in at least one application for finance over the three years prior the survey: this is the percentage of firms who applied for any type of finance in the three years prior to the survey and were turned down outright in at least one of their applications (base: total number of firms who applied for any kind of finance over the three years prior to the survey)⁷⁶.

⁷⁶ Some firms will have made several applications for finance. This measure counts a firm as turned down if it was turned down in any of its applications. It therefore includes businesses who were turned down in one application but were successful in another or several other applications for finance.

(2) Percentage of applications that were turned down outright over the three years prior to the survey: this is the percentage of individual applications made by firms in the three years prior to the survey that were turned down outright (base: total number of applications for all facilities made over the three years prior to the survey). This measure takes into account each application made by all firms and the overall percentage of these that were turned down.

(3) Percentage of firms that obtained none of the finance sought over the three years prior to the survey: this measure looks at the overall outcome for all firms that applied for finance over the three years prior to the survey by asking firms, taking into account all their applications for finance in the three years prior to the survey, what percentage of the overall amount they obtained (base: total number of firms who applied for any kind of finance over the three years prior to the survey).

(4) Percentage of firms that obtained none of the finance sought over the 12 months prior to the survey: this measure looks at the overall outcome for all firms that applied for finance over the 12 months prior to the survey by asking whether they obtained all, some, or none of the total amount sought. (base: total number of firms who applied for any kind of finance over the 12 months prior to the survey). This measure provides a more recent snapshot of supply than the other measures.

The results are presented for SMEs as a whole and, where sample sizes permit, for the following sub-groups⁷⁷: size band; risk rating; sector; location (urban/rural); and business type (exporter; high growth firms; and new starts⁷⁸).

This chapter also presents findings on the stage of the application process that SMEs were turned down or offered less finance to gain an understanding of any differences in reporting between the supply measures considered in this report and the approvals rates reported by financial providers. It also considers SMEs' perceptions of how the cost of credit and ease of access to finance had changed over the year prior to the survey.

7.1 Percentage of firms turned down outright in at least one application over the three years prior to the survey⁷⁹

7.1.1 All SMEs

The majority of SMEs (87 per cent) who applied for finance were successful in obtaining all the finance they needed. The proportion of SMEs turned down outright in at least one of their applications, at six per cent, was a quarter of what it was at its peak in 2010, indicating that credit conditions had improved significantly for SMEs. Just two per cent were turned down in each and every application.

⁷⁷ Please see methodology section for further detail on the definitions used within each sub group.

⁷⁸ Businesses may fall into more than one these three 'business type' categories. Six per cent of SMEs sampled were new starts (61 businesses), 13 per cent were high growth (60 businesses) and 22 per cent were exporters (261 businesses).

⁷⁹ It is not possible to provide results by sector, firm type or location for this measure given the low sample sizes involved.

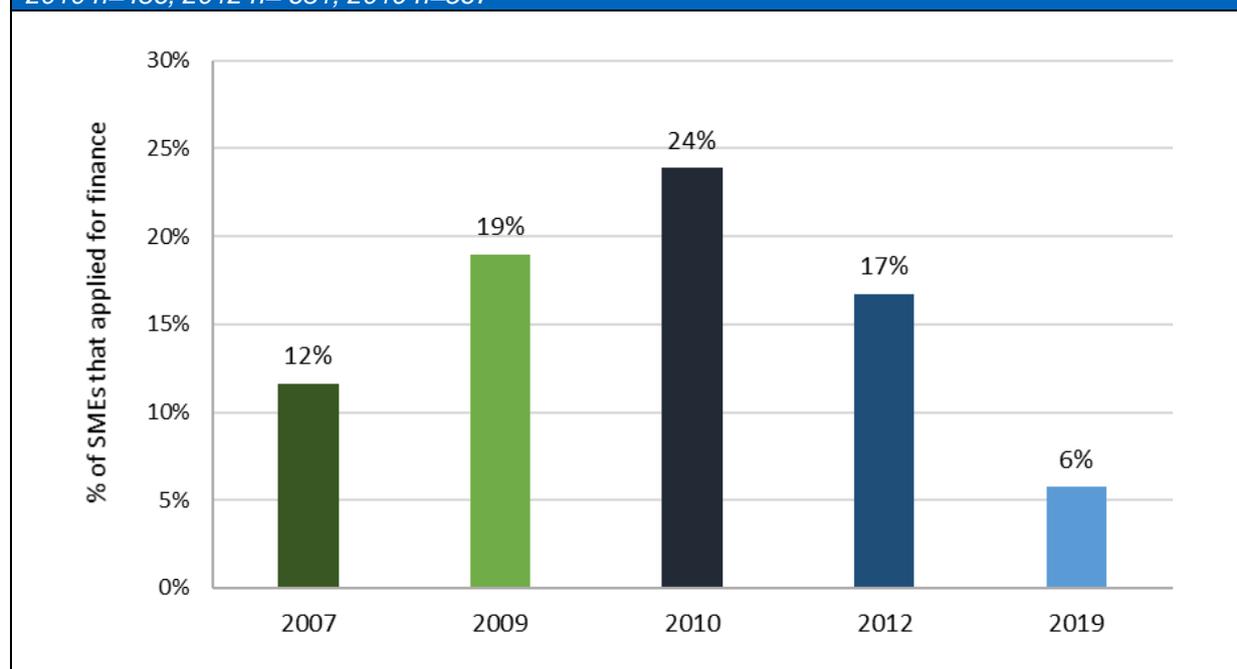
It is important to view the percentage of firms who were turned down outright in at least one of their applications in the context of the proportions who were offered exactly what they wanted and offered less than they wanted.

87 per cent of SMEs who applied for finance in the last three years were offered exactly what they wanted for each and every application for finance they made. 13 per cent were offered less or turned down outright in at least one of their applications.

Of that 13 per cent, 10 per cent were offered less in at least one of their applications and **6 per cent were turned down outright in at least one of their applications**⁸⁰. As illustrated in figure 13, the percentage of SMEs turned down outright in at least one of their applications for finance in 2019 was considerably lower than in prior years – lower, even, than before the financial crisis in 2007 – and was four times lower than the peak in 2010.

Figure 13: SMEs turned down outright in at least one of their applications for finance in the three years prior to the survey

Base: SMEs who applied for finance in the three years prior to the survey. 2007 n=250; 2009 n=631; 2010 n=486; 2012 n= 631; 2019 n=567



Of the 6 per cent of SMEs that were turned down in at least one of their applications for finance, just 2 per cent were turned down for each and every application for finance they made, receiving none of the finance they sought. As illustrated in figure 14, this proportion was considerably lower than in all previous years.

⁸⁰ The percentage turned down outright in at least one application and the percentage receiving less than wanted in at least one application does not sum to the percentage who said they were turned down or offered less as some firms will have been turned down for some applications and offered less for others

Figure 14: SMEs turned down outright in each and every application for finance in the three years prior to the survey

Base: SMEs who applied for finance in the three years prior to the survey. 2007 n=250; 2009 n=631; 2010 n=486; 2012 n= 631; 2019 n=567

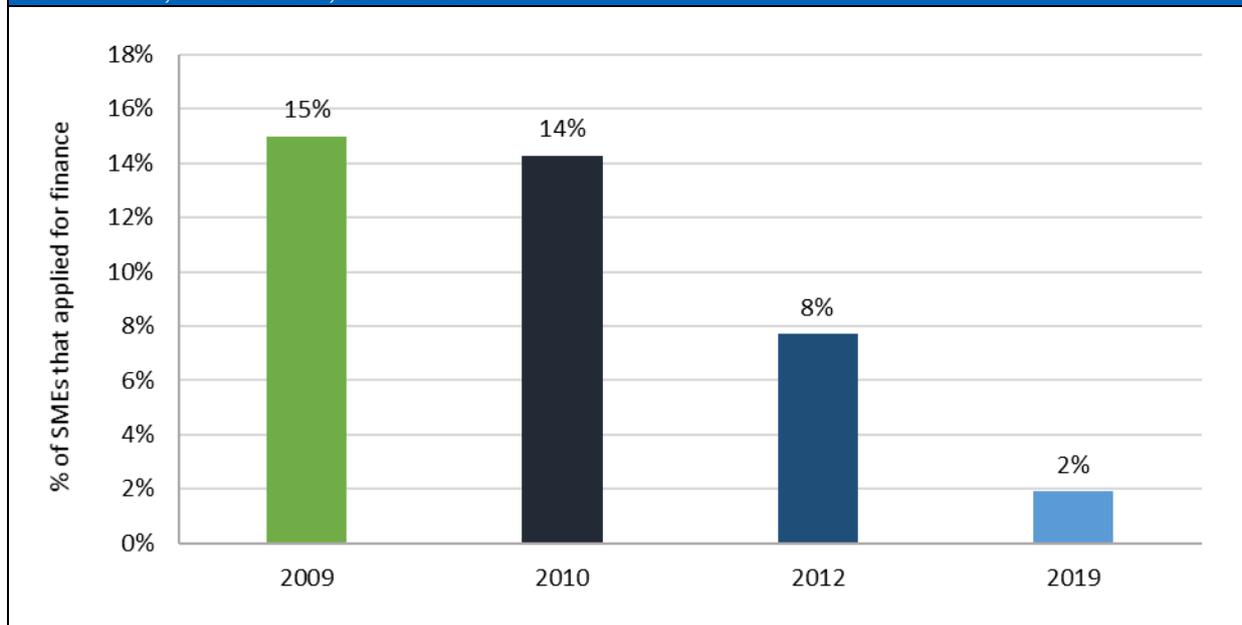


Figure 15 illustrates the results by finance type, showing the percentage of SMEs who applied for finance in the past three years that were: turned down outright; offered less than they wanted; and offered exactly what they wanted.

SMEs were less likely to receive all the finance they sought for unsecured loans

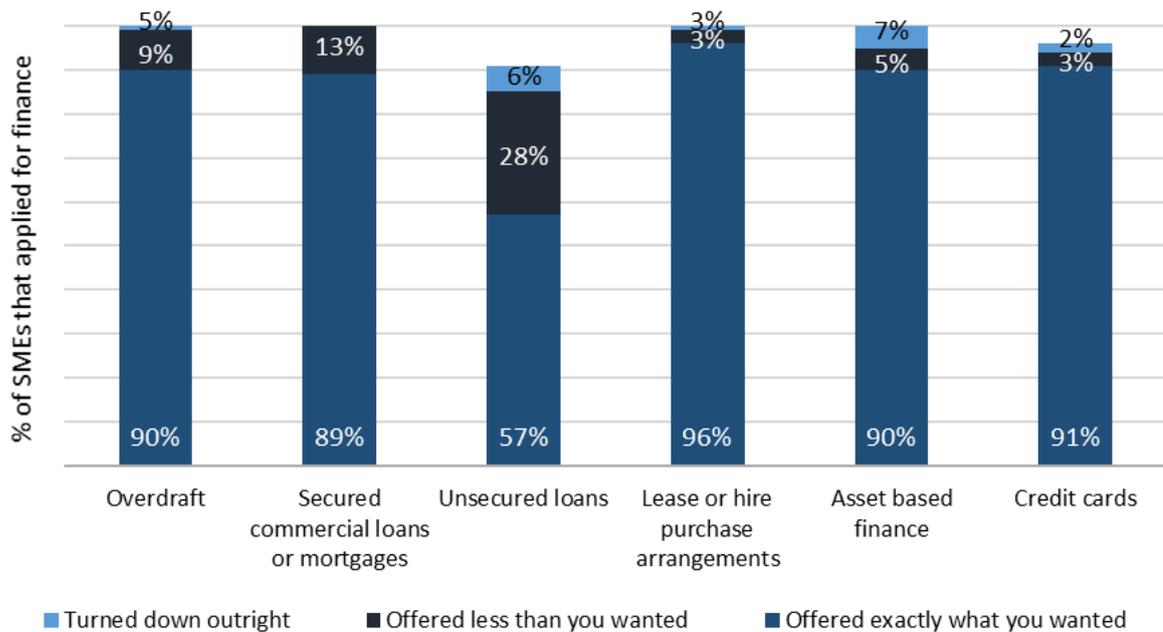
The proportion of firms that were turned down outright was broadly similar across the finance types⁸¹. However, the proportion of firms that were offered less than what they wanted was higher than average for unsecured loans (28 per cent) and lower than average for lease/HP and credit cards (both 3 per cent).

The proportion of firms stating that they were offered exactly what they wanted was broadly similar across most finance types, with the exception of unsecured loans. Just over half (57 per cent) of the business applying for unsecured loans said they were offered exactly what they wanted compared to around nine in ten firms for all other finance types. This makes sense given it is a riskier type of finance for the lender.

⁸¹ While there are some apparent differences between finance types, the results are not statistically significantly different to that for all finance types, likely due in part to the small sample sizes involved.

Figure 15: Percentage of SMEs that applied for finance in the three years prior to the survey that were turned down outright, offered less than wanted and offered exactly what they wanted, by finance type (note small sample sizes)⁸²

Base: SMEs who applied for finance type in the three years prior to the survey (overdraft n=286; secured loans/mortgages n=56; unsecured loans n=54; lease/HP n=223; asset based n=58; credit cards n=129 (not shown: crowd funding n=2; equity n=9)



7.1.2 Size band

Somewhat surprisingly, medium-sized businesses were more likely to have experienced rejection.

Considering findings by business size band, somewhat surprisingly, medium-sized firms were more likely than average to have experienced at least one instance of rejection at 20 per cent. Medium-sized firms were more likely to apply for finance and to make multiple applications so it may be that within they were therefore more likely to have “marginal” applications rejected.

The proportions of micro and small businesses that were turned down in at least one application were broadly in line with the results for SMEs as a whole, likely due in part to the small sample sizes involved.

⁸² The results for equity finance and crowd funding are not shown here as the sample sizes are too low (below 10). The figures do not sum to 100%. Where results sum to less than 100%, this is because those businesses answering ‘don’t know’ are not shown. Where results sum to more than 100%, this is because there appears to have been instances of businesses answering ‘yes’ to multiple options within each finance type for example a business saying that they were offered exactly what they wanted and also that they were offered less than they wanted. This may have been the case if a business had made more than one application for each finance type.

7.1.3 Risk rating

Lower risk rated businesses were also more likely to have experienced rejection

Considering findings by the business' risk rating, again somewhat surprisingly, firms with a risk rating of 'minimum' (the lowest risk rating) were more likely than average to have experienced at least one instance of rejection at 14 per cent. As with the findings for medium-sized firms, this seems counter-intuitive. However, as shown in section 7.3.3, the lowest risk rated firms were more likely than average to receive all the finance they sought.

The proportions of businesses with low, average and above average risk ratings that were turned down in at least one application were broadly in line with that for SMEs as a whole, likely due in part to the small sample sizes involved.

It is not possible to provide results by sector, firm type or location for this measure given the low sample sizes involved.

7.2 Percentage of applications that were rejected outright in the three years prior to the survey⁸³

7.2.1 All SMEs

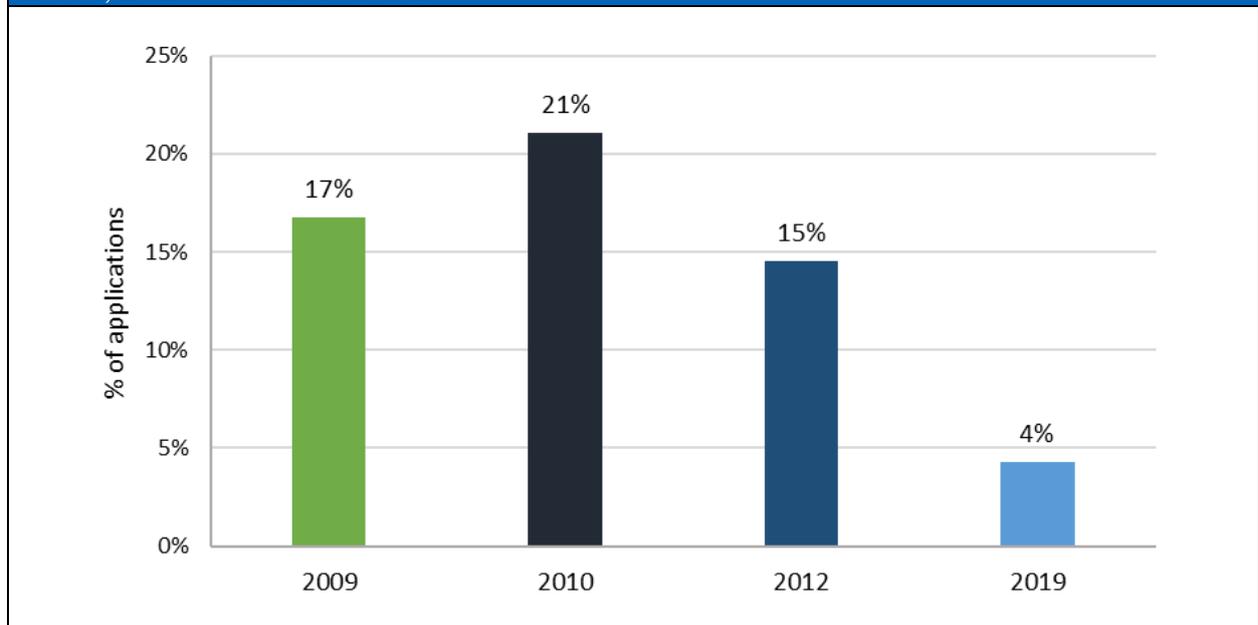
The majority of applications for finance (89 per cent) made by SMEs were successful. The proportion of applications for finance that were rejected outright, at four per cent, was less than a fifth of what it was in 2010, again indicating that credit conditions have improved significantly.

In 2019, 89 per cent of applications made for finance in the three years prior to the survey were successful. In eight per cent of applications, SMEs were offered less than the amount of finance they sought and just four per cent of applications were rejected outright. The proportion of applications rejected outright in 2019 was considerably lower than in all previous years and five times lower than at its peak in 2010 (Figure 16).

⁸³ It is not possible to provide results by location for this measure.

Figure 16: Percentage of applications rejected over the three years prior to the survey

Base: Number of applications for finance over the three years prior to the survey: 2009 n=1290; 2010 n= 904; 2012 n=1268 2019 n=1048



7.2.2 Size band

Medium-sized businesses were more likely to have had an application turned down

In line with the findings for the percentage of firms that were turned down, the application rejection rate for applications made by medium-sized firms was higher than average, at 19 per cent. Again, this seems counter-intuitive.

The proportions of applications made by micro and small businesses that were turned down were broadly in line with the results for SMEs as a whole.

7.2.3 Risk rating

Lower risk rated businesses were more likely to have had an application turned down

In line with the findings for the percentage of firms that were turned down, the application rejection rate for applications made by firms with a risk rating of 'minimum' (the lowest risk rating) was higher than average at 8 per cent. Again, this seems counter-intuitive.

The proportions of applications made by businesses with low, average and above average risk ratings that were turned down were broadly in line with that for SMEs as a whole.

7.2.4 Sector

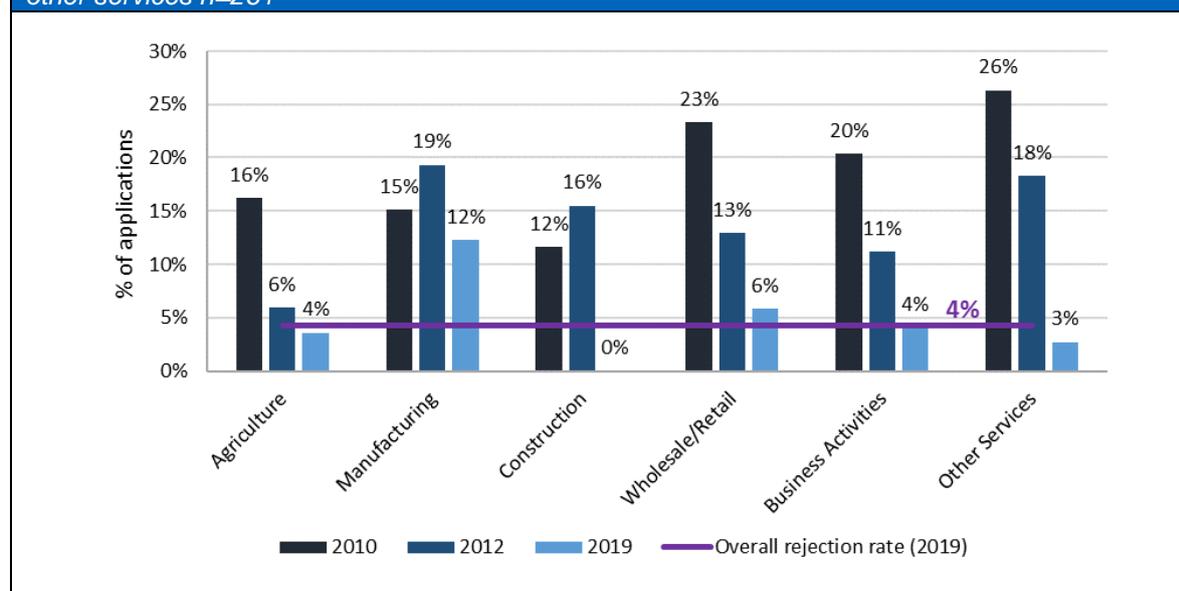
The manufacturing sector had a higher than average rate of application rejections which had not improved significantly relative to 2010

In 2019, the application rejection rate was higher than average for firms in the manufacturing sector (12 per cent) and lower than average for the construction sector (0 per cent). All other sectors were broadly in line with the average for all firms (Figure 17).

Relative to 2012, the construction, business activities and other services sectors all saw a considerable improvement in the application rejection rate⁸⁴. Relative to 2010, all sectors, with the exception of manufacturing⁸⁵, saw a significant improvement in the application rejection rate.

Figure 17: Percentage of applications rejected, by sector

Base: Number of applications for finance made in last three years. 2019: Agriculture n=94; manufacturing n=71; construction n=145; wholesale/retail n=111; business services n=250; other services⁸⁶ n=373. 2012: Agriculture n=105; manufacturing n=170; construction n=154; wholesale/retail n=286; business services n=232; other services n=231. 2010: Agriculture n=92; manufacturing n=171; construction n=120; wholesale/retail n=127; business services n=133; other services n=261



7.2.5 Business type

Exporters and new starts saw an improvement in application rejection rates relative to 2010.

In 2019, the application rejection rate for high growth, exporter and new start firms were all broadly in line with the figure for firms as a whole. While the rejection rates

⁸⁴ For all other sectors, while the data shows there was a fall, the change from 2012 is not statistically significant.

⁸⁵ While the data shows there was a fall in the application rejection rate for manufacturing, the change from 2010 is not statistically significant.

⁸⁶ The 'other services' sector combines: hotels; transport; health/social work; other services.

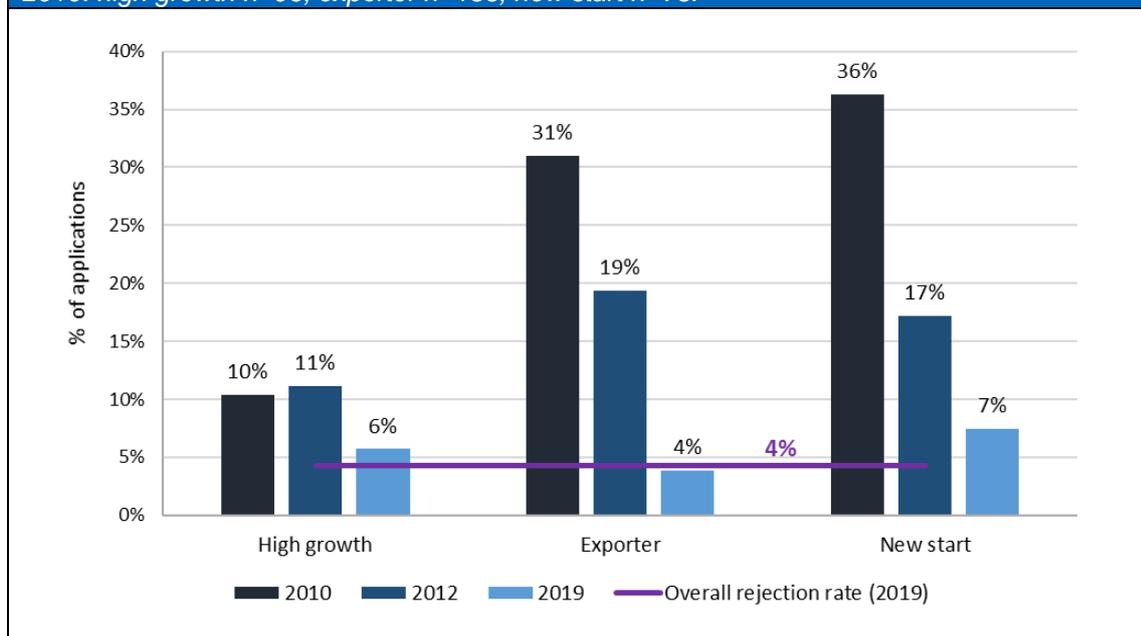
for high growth (6 per cent) and new start (7 per cent) firms appear to be higher, the difference with the figure for all firms (4 per cent) is not statistically significant due to the small sample sizes involved (Figure 18).

Relative to 2012, only exporters saw a statistically significant improvement in the application rejection rate⁸⁷. Relative to 2010, both exporters and new starts saw a statistically significant improvement in the application rejection rate.

It is not possible to provide results by location for this measure.

Figure 18: Percentage of applications rejected, by business type

Base: Number of applications for finance made in last three years. 2019: high growth n=80; exporter n=285; new start n=58. 2012: high growth n=73; exporter n=279; new start n=132. 2010: high growth n=96; exporter n=186; new start n=73.



7.3 Percentage of firms that obtained none of the finance sought over the three years prior to the survey

7.3.1 All SMEs

Eight in ten SMEs received all the finance they sought over the three years prior to the survey. The proportion that received none of the finance they sought, at one in ten, was a quarter of what it was at its peak in 2009, again indicating a significant improvement in credit conditions.

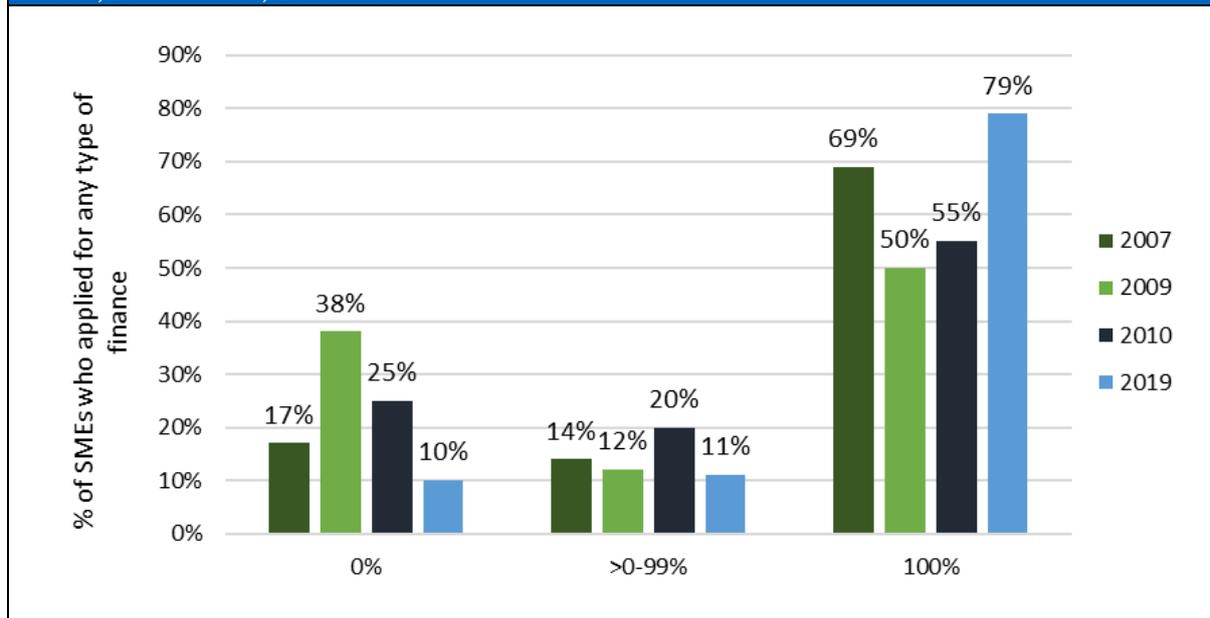
Considering all the finance they applied for overall in the three years prior to the survey, firms were asked what proportion of the overall amount they obtained on a scale of 0 per cent (none was granted) to 100 per cent (all was granted) (Figure 19). In 2019, 79 per cent of SMEs who applied for finance in the three years prior to the survey said they received all they sought, higher than the pre-crisis proportion in

⁸⁷ For new starts and high growth firms, while the data shows there was a fall, the change from 2012 is not statistically significant due to the small sample sizes involved.

2007 (69 per cent). **10 per cent of SMEs who applied for finance stated that they received none (0 per cent) of the finance they sought**, considerably lower than the proportion in prior years⁸⁸. 11 per cent said they received some of the finance sought. Of that 11 per cent, 3 per cent said they received 76-99 per cent of the total amount sought, 3 per cent received 51-75 per cent, 2 per cent received 26-50 per cent, 1 per cent received 10-25 per cent and 1 per cent received less than ten per cent⁸⁹.

Figure 19: Overall success in securing finance sought over the three years prior to the survey

Base: SMEs who applied for finance in the three years prior to the survey. 2007 n=250; 2009 n=631; 2010: n=486, 2019 n=567



7.3.2 Size band

Medium-sized firms were more likely to receive finance while small firms were less likely to receive 100 per cent of the finance sought

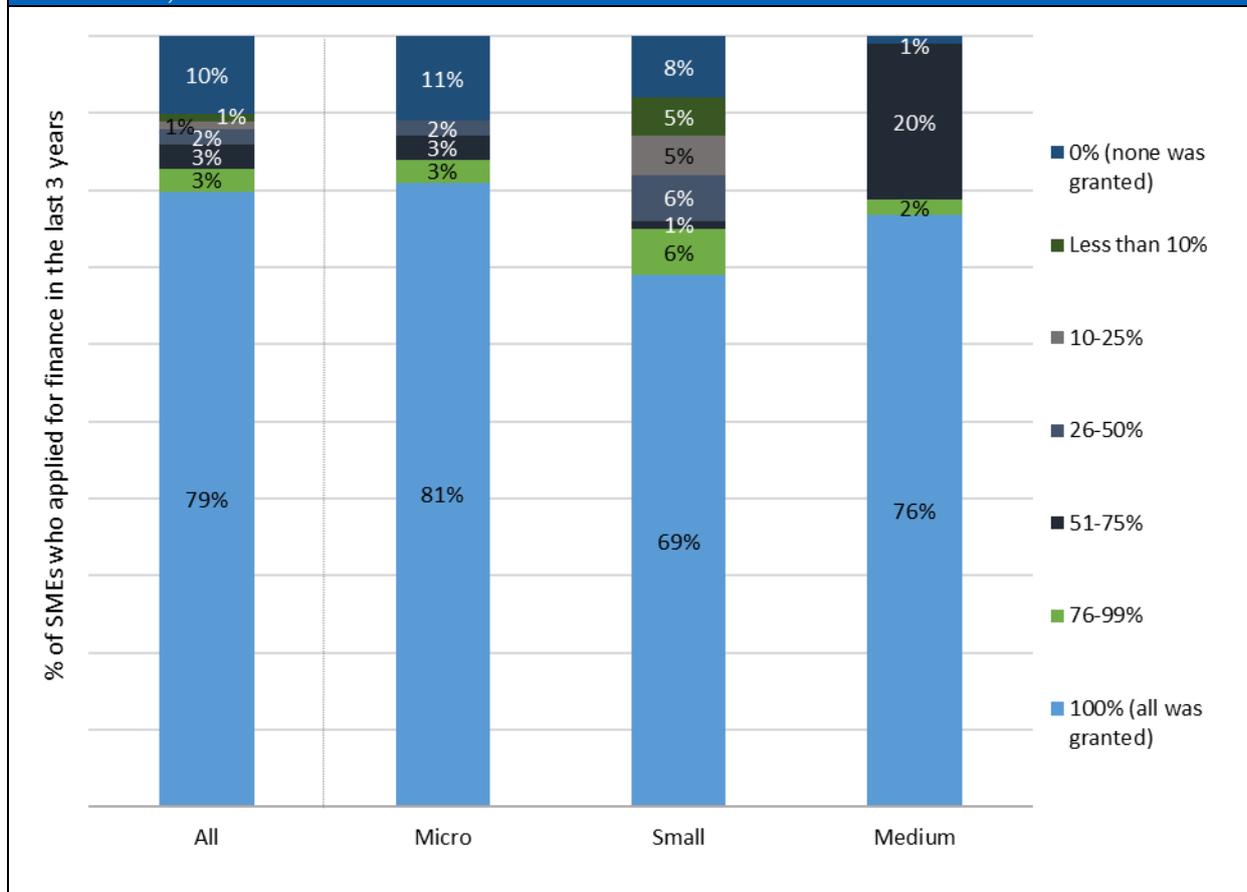
Figure 20 illustrates the findings by firm size band. Despite being more likely to have experienced rejection (see sections 7.1.2 and 7.2.2), medium-sized firms were more likely than average to receive at least some finance (more than 0 but less than 100 per cent) of the finance sought. Small firms were less likely than average to receive all of the finance they sought.

⁸⁸ It is not possible to compare with 2012 due to a change in the way this question was asked in that year. For comparability with prior years analysis, those firms stating 'don't know' were removed from this question.

⁸⁹ Individual percentages do not sum to 11 per cent due to rounding.

Figure 20: Overall success in securing finance sought over the three years prior to the survey, by firm size

Base: SMEs who applied for finance in the three years prior to the survey. All n=567; micro n=231; small n=252; medium n=84



7.3.3 Risk rating

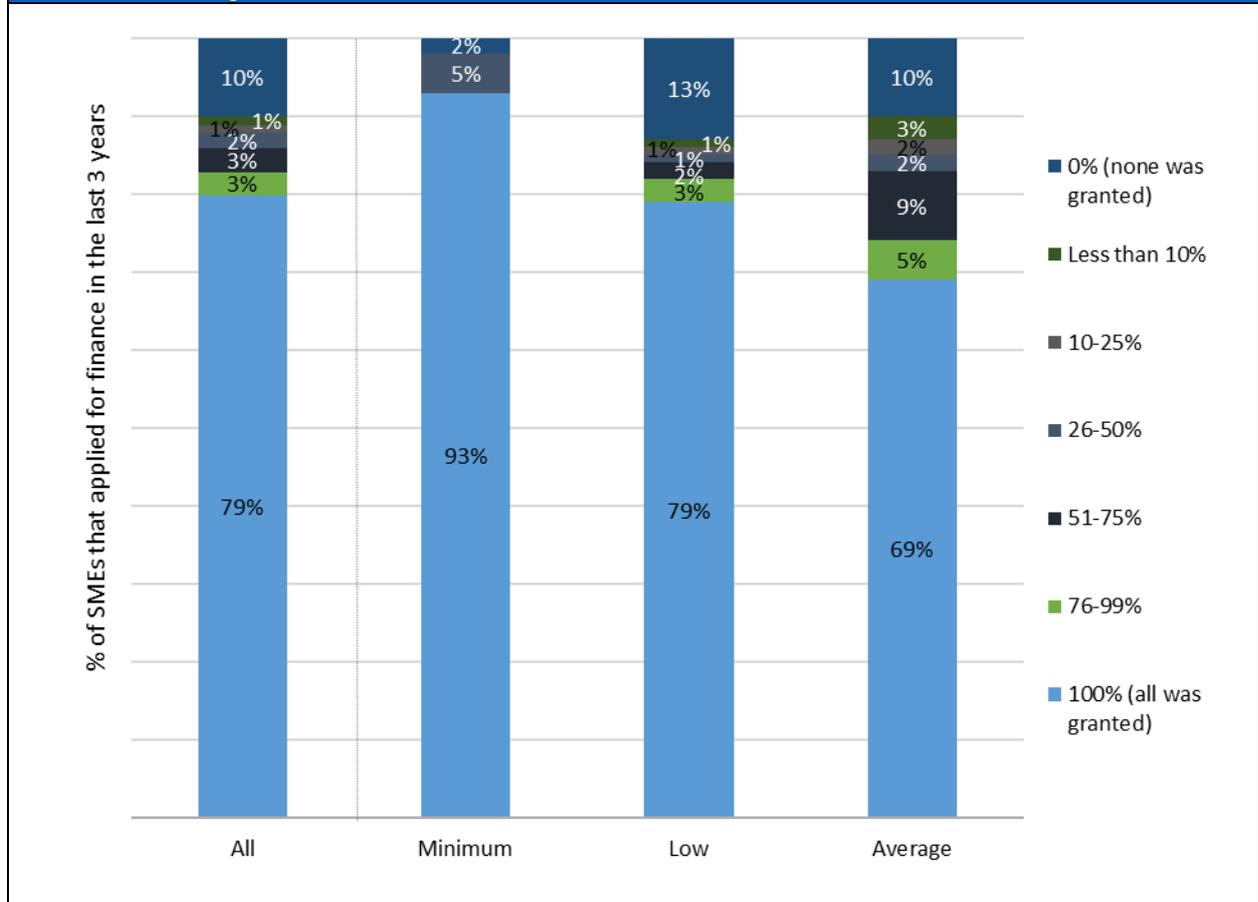
Lower risk firms were more likely to receive all the finance they sought

Firms with lower risk ratings were more likely to receive all the finance they sought, despite being more likely to have experienced rejection (see sections 7.1.3 and 7.2.3). Firms with a minimum risk rating (the lowest risk rating) were more likely than average to receive all the finance they sought (93 per cent compared to the all firm average of 79 per cent) and less likely to receive none (2 per cent compared to the all firm average of 10 per cent). Firms with an 'average' risk rating were less likely than average to receive all of the finance they sought (69 per cent compared to the all firm average of 79 per cent). The findings for firms with an above average risk rating are not reliable given the low sample size and therefore not shown in figure 21⁹⁰.

⁹⁰ Just 11 firms surveyed had an 'above average' risk rating.

Figure 21: Overall success in securing finance sought in the three years prior to the survey, by risk rating

Base: SMEs who applied for finance in the three years prior to the survey. All n=567; minimum n=110 low n=285; average n=114⁹¹



7.3.4 Sector

The agriculture sector was the most successful in obtaining the full amount of finance sought whilst the construction sector was the least successful

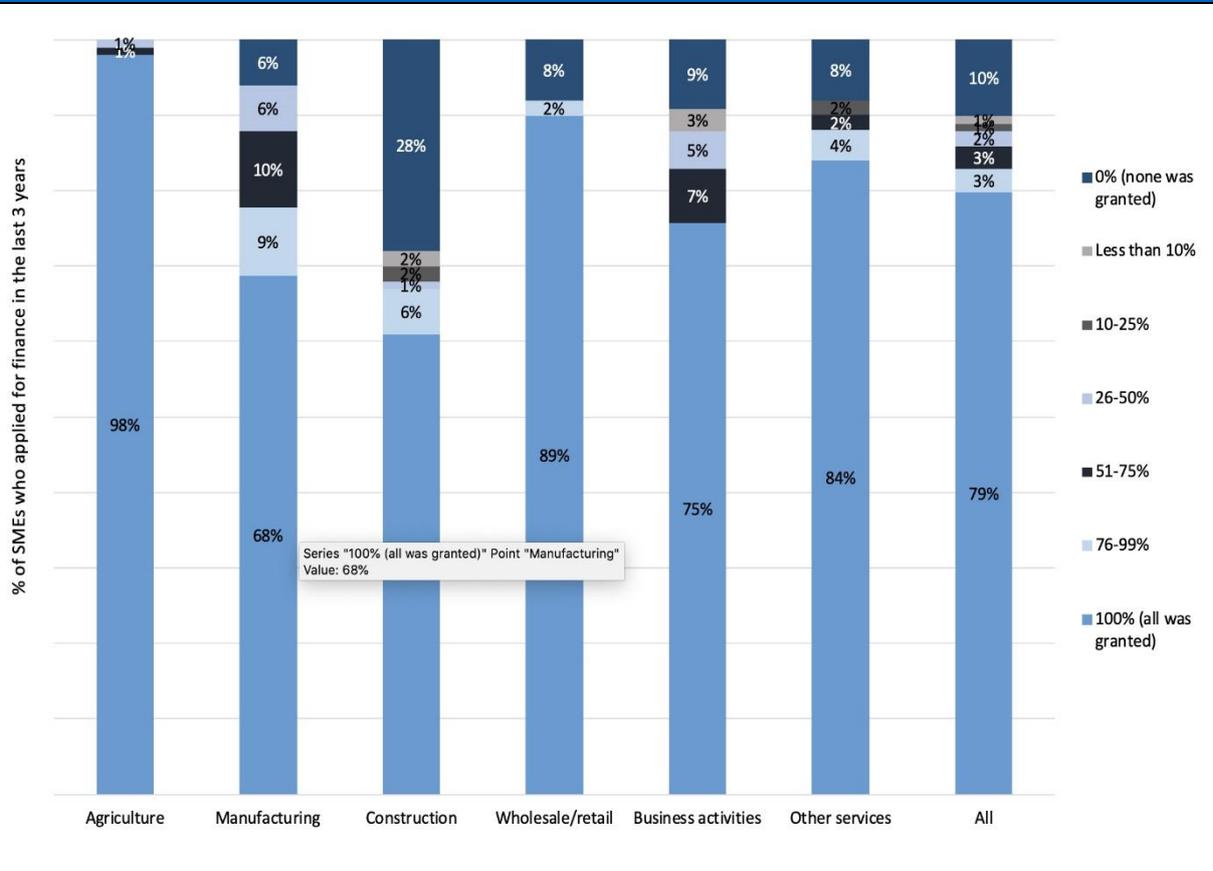
Firms in the agriculture sector were more likely than average to receive the full amount of the finance they sought and less likely to receive nothing (Figure 22). In contrast, firms in the construction sector were significantly more likely than average to receive nothing and less likely than average to receive the full amount of finance they sought.

For all other sectors, the proportion of firms receiving 0% and 100% of the finance sought was broadly in line with the average. This is in part due to the small sample sizes for some sectors which mean that apparent differences between a sector and the average for all SMEs are not statistically significant.

⁹¹ The findings for firms with 'above average' risk rating are not shown as the sample size (n=11) is too small to provide reliable results.

Figure 22: Overall success in securing finance sought in the three years prior to the survey, by sector

Base: SMEs who applied for finance in the three years prior to the survey. All n=567; agriculture n=46; manufacturing n=33; construction n=85; wholesale/retail n=66; business activities n=129; other services n=207.



7.3.5 Business type

Exporters were less likely than SMEs as a whole to receive none of the finance they sought

In 2019, exporters were less likely than SMEs as a whole to receive none of the finance they sought⁹². It is not possible to provide reliable results of high growth firms or new starts due to the small sample sizes involved.

7.3.6 Urban/rural location

Rural SMEs were more likely than average to receive the full amount of finance sought, likely driven by the prevalence of the agriculture sector in rural areas, which saw the highest success rates of all the sectors.

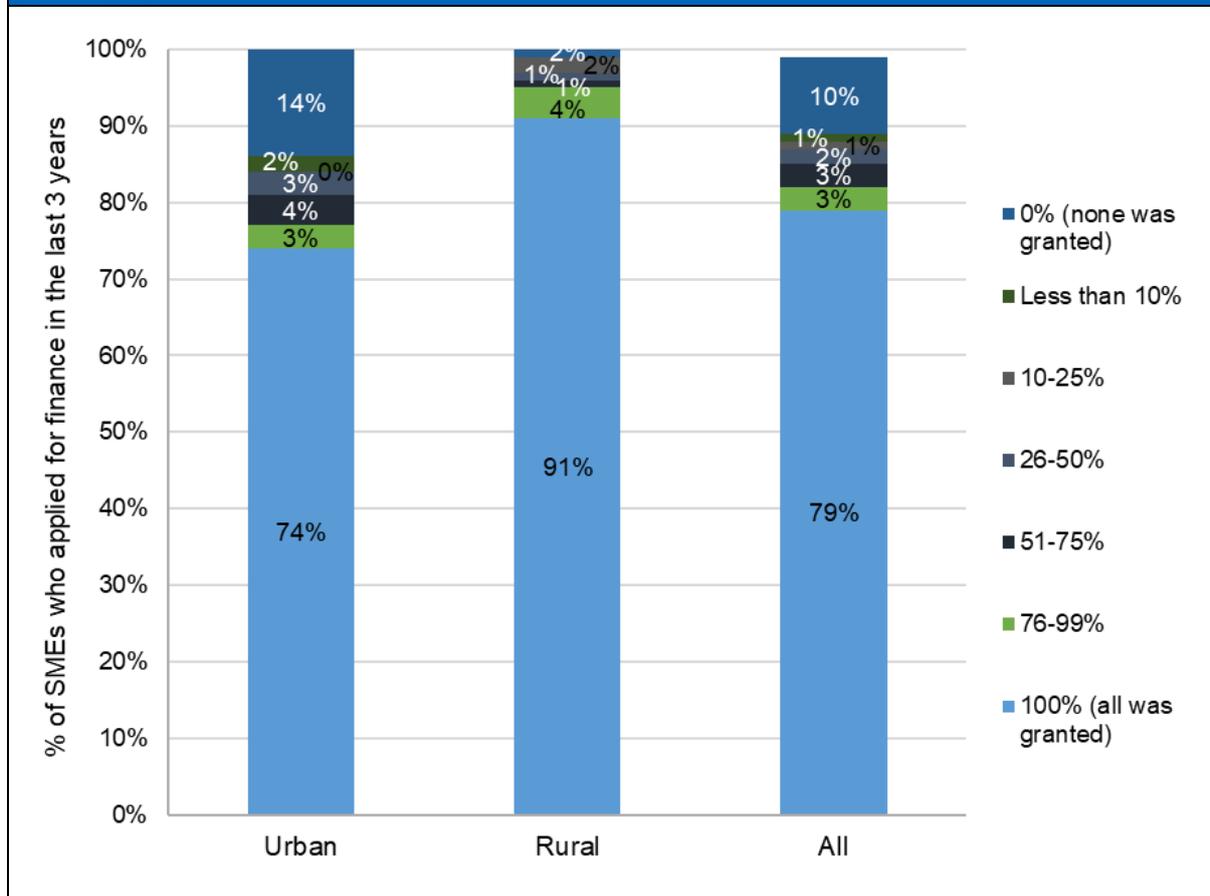
Rural SMEs were more likely than average to receive 100 per cent of the finance they sought, at 90 per cent (Figure 23). Just one per cent of rural firms received none of the finance they sought. This reflects the sectoral results where agriculture

⁹² For all other proportions of finance sought that were obtained, the results for exporters were not statistically significantly different to those for all SMEs.

firms, prevalent in rural areas, saw the highest success rates. The results for urban firms were not statistically significantly different to the all firm average.

Figure 23: Overall success in securing finance sought over the three years prior to the survey, by location

Base: SMEs who applied for finance in the three years prior to the survey. All n=567; urban n=373; rural n=194



7.4 Percentage of firms that obtained none of the finance sought over the 12 months prior to the survey⁹³

The three measures of supply considered so far all considered the finance sought by SMEs over the three years prior to the survey. To provide a more recent snapshot of supply conditions, SMEs who had sought new finance over the 12 months prior to the survey were asked whether they obtained all, some or none of the finance they sought over this period.

⁹³ It is not possible to provide disaggregated results for this measure.

7.4.1 All SMEs

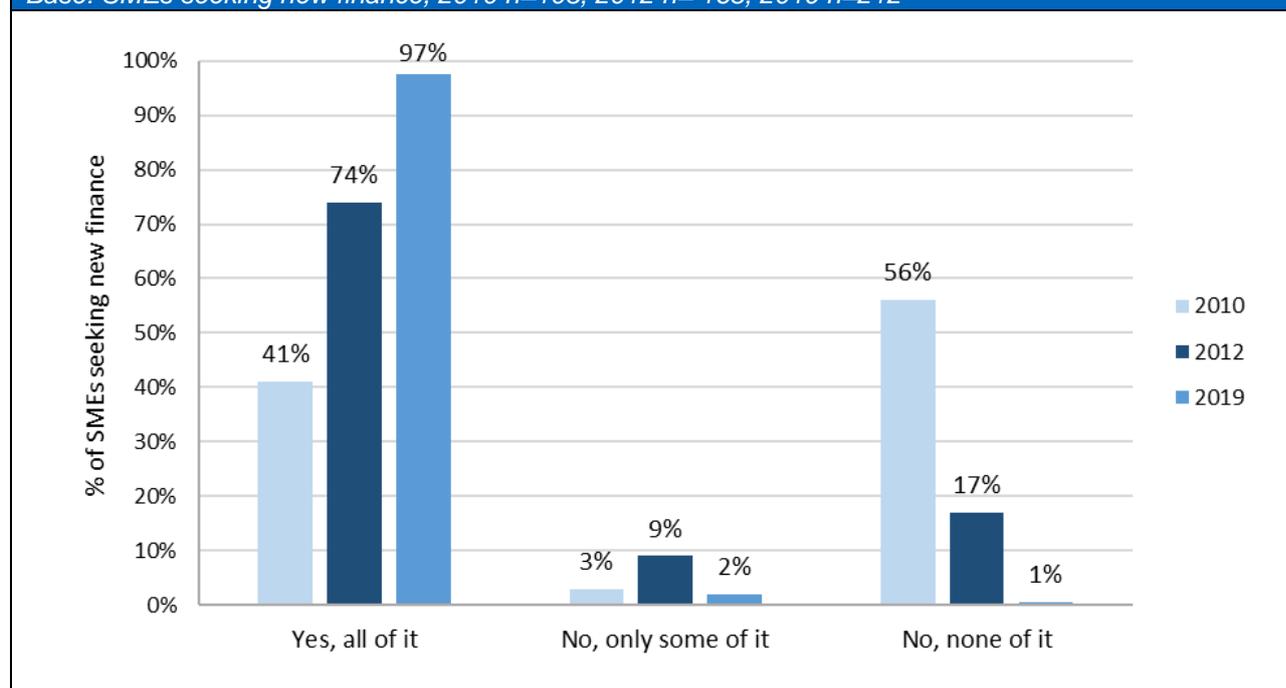
Almost all (97 per cent) SMEs secured all the finance they sought over the 12 months prior to the survey. The proportion that received none of the finance they sought, at less than one per cent, had fallen from over half in 2010.

97 per cent of SMEs who sought new finance in the last 12 months secured all the finance they sought⁹⁴. The proportion of SMEs that were successful in obtaining all of the finance sought had more than doubled from the proportion in 2010 (41 per cent) (Figure 24). Only two per cent of SMEs seeking new finance secured just some of the finance they sought. **Less than one per cent secured none of the finance sought over the 12 months prior to the survey**, down from over half of all firms in 2010, again indicating that credit conditions had improved considerably for SMEs over this period.

The proportion of SMEs securing the full amount sought over the 12 months prior to the survey (97 per cent) was higher than that over the three years prior to the survey (79 per cent), suggesting credit conditions improved further over 2019.

Figure 24: Amount of new finance successfully obtained over the 12 months prior to the survey⁹⁵

Base: SMEs seeking new finance, 2010 n=103; 2012 n= 168; 2019 n=212



⁹⁴ In line with previous years of the survey, the responses for this question were rebased to remove those stating 'don't know'.

⁹⁵ Data is not available prior to 2010 as this question was introduced for the first time in 2010.

7.5 Stage of rejection in the application process

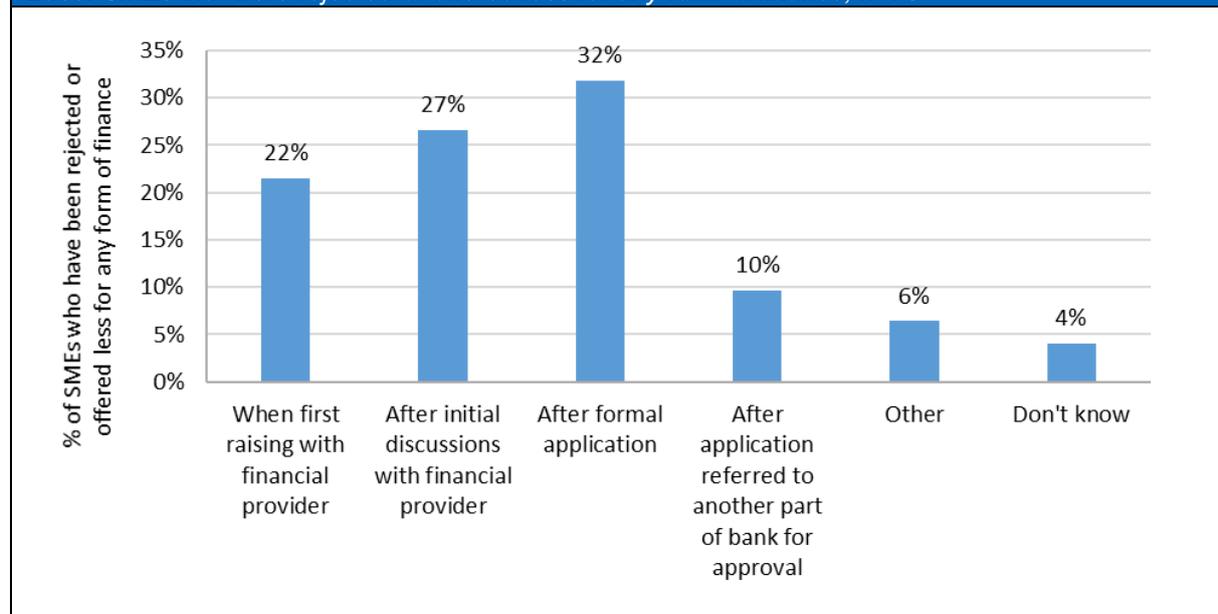
The measures of supply considered in the previous sections provide a different insight to approval rates reported by financial providers, which tend to be based on formal applications made and therefore do not consider those SMEs who are turned down before this stage. This short section examines the stage of the application process that SMEs that were turned down/offered less to determine the likely extent of any differences in reporting. It is important to note the small sample sizes involved in this question due to the small numbers of firms that were turned down/offered less in 2019.

Nearly half of SMEs who were turned down or offered less in any of their applications for finance were turned down/offered less at the initial stages, before a formal application was made, suggesting a significant amount of unmet demand will not be reflected in financial providers' approval rates. However, given the low proportion of SMEs that were turned down/offered less in 2019, any difference is likely to be minimal.

SMEs who had been rejected/offered less in any of their applications for finance over the three years prior to the survey were asked, for their largest application, at what stage in the process they were turned down/offered less (Figure 25). Nearly half (48 per cent) were turned down/offered less at the initial stages, before a formal application had been made. This was broadly in line with the proportion in 2010 (49 per cent) and 2012 (46 per cent) and suggests a significant proportion of unmet demand will not be reflected in financial providers' approval rates. However, given the low proportion of SMEs that were turned down/offered less in 2019, any difference is likely to be minimal.

Figure 25: Stage of application process rejected or offered less

Base: SMEs that were rejected or offered less for any form of finance, n=73



7.6 Costs and ease of access to finance

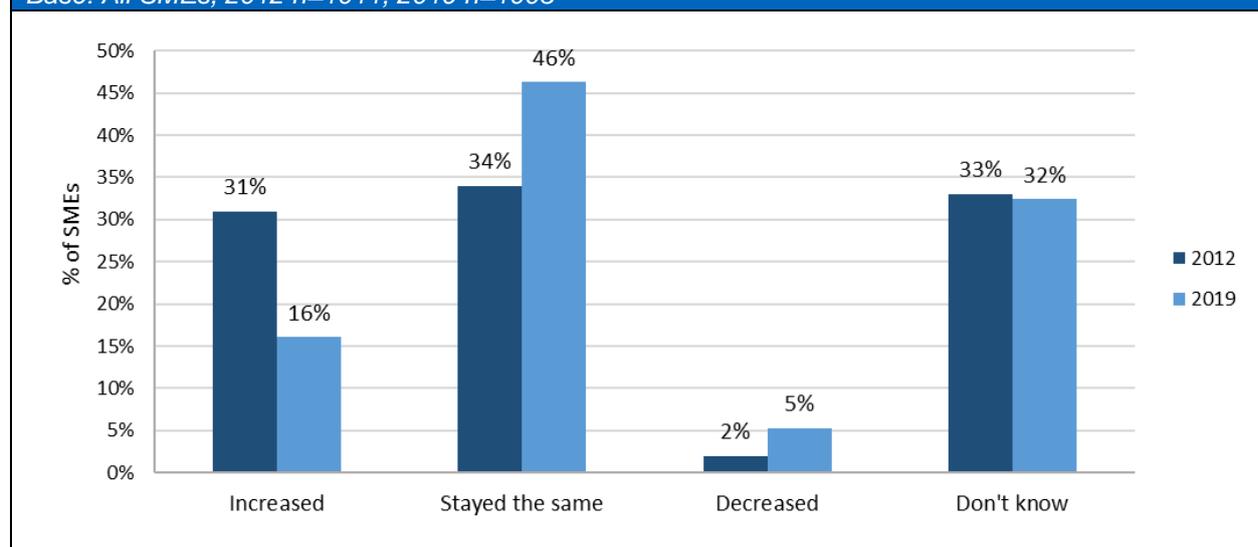
The proportion of SMEs reporting an increase in the cost of credit had halved since 2012

All SMEs were asked whether they felt there had been an increase in the overall cost of new credit over the 12 months prior to the survey (Figure 26). 16 per cent of SMEs felt the cost of credit had increased, almost half of the proportion in 2012. Almost half of SMEs surveyed in 2019 thought the cost of credit had stayed the same (up from a third of businesses in 2012) while five per cent felt it had decreased.

Those who felt they had seen an increase in the cost of credit (193 businesses) were asked what types of facility they thought had become more expensive. The most commonly cited facility was overdrafts (cited by 56 per cent SMEs who saw an increase in the overall cost of credit), followed by credit cards (33 per cent), secured loans (33 per cent) and unsecured loans (27 per cent).

Figure 26: Perception of change in cost of new credit over 12 months prior to survey

Base: All SMEs, 2012 n=1011; 2019 n=1003

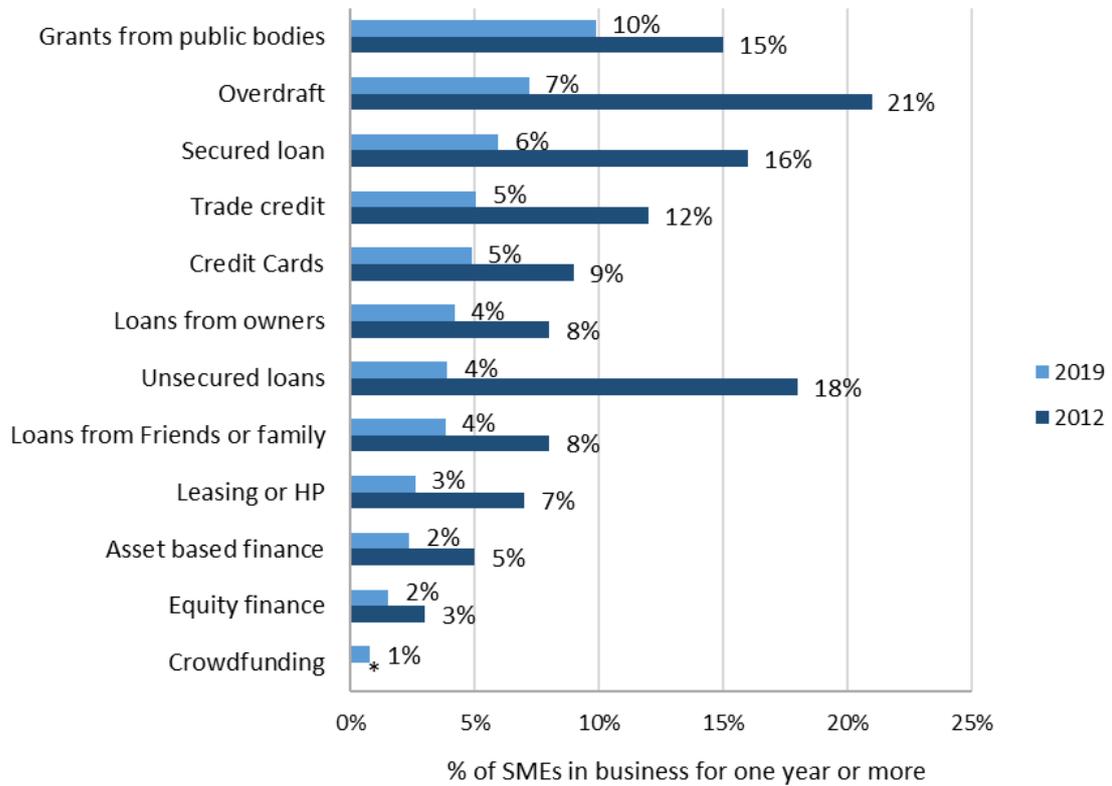


Perceptions of ease of access to finance have improved across all finance types relative to 2012

All SMEs in business for one year or more were asked whether they felt access to each type of finance for their business has stayed the same, become harder or easier compared to a year previously. Across all forms of finance, the proportion reporting that finance was harder to access was less than ten per cent and lower than the proportion in 2012. The finance type with the highest proportion of SMEs reporting that access was harder was grants from public bodies. Compared to 2012, overdrafts and unsecured loans saw the largest drop in the proportion of SMEs that reported access to finance was harder (Figure 27).

Figure 27: Forms of finance harder to access compared to a year ago

Base: SMEs in business for one year or more, 2012 n=957; 2019 n=947



8. Abilities in applying for finance and use of external advice

Summary

- Just over half of SMEs felt confident in their understanding of the different forms of external finance available to the business. SMEs felt more confident in their ability to put together an application to obtain finance from their main bank than other providers. This echoes the results in chapters 4 and 5 that most SMEs rely on their main bank for most of their finance needs and indicates there may be a need to improve SMEs' understanding of the range and benefits of the various financial products and providers available.
- Just over a third of SMEs sought external advice when considering or applying for finance and the most common sources of advice were the business's accountant/financial adviser and their main bank, suggesting there may be a need to encourage greater use of independent external advice.

As discussed in section 1.3, market failures can occur on the demand side which mean that businesses do not seek an optimal amount of external finance. This may be due to businesses failing to fully understand the benefits of using external finance, how to access the variety of external finance available, or which type might be most suited to their situation. Businesses may also lack the skills to present their propositions to provide lenders with a full understanding of their viability. To obtain an understanding of the extent to which these kinds of issues are at play amongst Scottish SMEs, a number of new questions were added to the 2019 survey. The results are presented for SMEs as a whole and also, where possible, for key sub-groups of interest including size band, sector, business type (high growth/exporter/new start) and location (urban/rural).

8.1 Abilities in applying for finance

Just over half of SMEs felt confident in their understanding of the different forms of external finance available to the business. SMEs felt more confident in their ability to put together an application to obtain finance from their main bank than other providers

Over half (57 per cent) of SMEs felt **confident in their understanding of the different forms of external finance available** to their business. Confidence increased with business size, with small and medium sized businesses more confident than average (Table 3).

Exporters (66 per cent) and manufacturing firms (76 per cent) were also more confident than average in their understanding of the various finance types available to them⁹⁶. The results by location were in line with the all-firm average.

⁹⁶ For all other firm types and sectors, the proportion reporting they were confident was broadly in line with the all-firm average.

Table 3: Abilities in applying for external finance: Percentage of firms stating they are confident⁹⁷ in their abilities in each area

Base: All SMEs, 1003 (0-9 employees n=494; 10-49 employees n=387, 50-249 employees n=122)

	All	Micro	Small	Medium
Confident in your understanding of the different forms of external finance available to you and your business	57%	54%	75%	98%
Confident in your ability to put together an application to obtain external finance from your main bank	73%	71%	88%	87%
Confident in your ability to put together an application to obtain external finance from someone other than your main bank?	61%	59%	74%	86%

SMEs as a whole were more **confident in their ability to put together an application to obtain finance from their main bank** (73 per cent) than **other providers** (61 per cent), echoing the results in chapters 4 and 5 that most SMEs rely on their main bank for most of their finance needs. Small and medium-sized businesses were more confident in their abilities in putting together applications than the all-firm average.

Exporters were also more confident than average in their abilities in putting together an application to obtain finance from their main bank (83 per cent) and from other providers (70 per cent).

By sector, firms in the wholesale/retail sector (62 per cent) were less confident than average in putting together an application for their main bank. In terms of applications for other providers, firms in the agriculture sector (45 per cent) were less confident than average, reflecting while firms in the business services sector (75 per cent) were more confident⁹⁸.

Looking at the findings by location, rural firms were less confident than average in their abilities in putting together an application for their main bank (65 per cent) and from other providers (47 per cent), reflecting the results on the lower confidence of the agriculture sector, prevalent in rural areas, in applying for finance. While rural SMEs were less confident in putting together an application, they were more likely than average to receive the full amount of finance sought (see section 7.3.6).

⁹⁷ Businesses are reported as confident if they responded 'fairly confident' or 'very confident'.

⁹⁸ For all other firm types and sectors, the proportion reporting they were confident was broadly in line with the all-firm average.

8.2 Use of external advice

Just over a third of SMEs sought external advice when considering or applying for finance and the most common sources of advice were the business's accountant/financial adviser and their main bank, suggesting there may be a need to encourage greater use of independent external financial advice.

Around a third (36 per cent) of SMEs that considered or applied for external finance in the last three years sought external advice⁹⁹ (Figure 28). The proportion of medium-sized firms that sought advice (62 per cent) was almost twice the all-firm average¹⁰⁰. High growth firms (57 per cent) and rural firms (49 per cent) were also more likely than average to seek advice. Looking at the sectors, firms in the manufacturing (65 per cent) and agriculture (61 per cent) sectors were more likely to have sought advice while firms in the construction sector (13 per cent) were less likely than average to have sought advice.

The most common source of external advice was from the business's accountant/financial adviser, cited by 47 per cent of SMEs who sought external advice, followed by the business's main bank (25 per cent). These two sources were the top two most common across all business size bands. Only nine per cent sought advice from Public Bodies such as Business Gateway, Scottish Enterprise and Highlands and Islands Enterprise. Looking at the results by location, the most common sources of advice for urban firms were accountant/financial adviser (54 per cent), public bodies (13 per cent) and main bank (12 per cent) whilst the most common sources for rural firms were their main bank (44 per cent), accountant/financial adviser (36 per cent) and 'other' (11 per cent)¹⁰¹. For rural firms, this underlines the findings around the importance of a local branch to their business.

⁹⁹ 63 per cent of SMEs that considered or applied for external finance did not seek external advice and one per cent did not know.

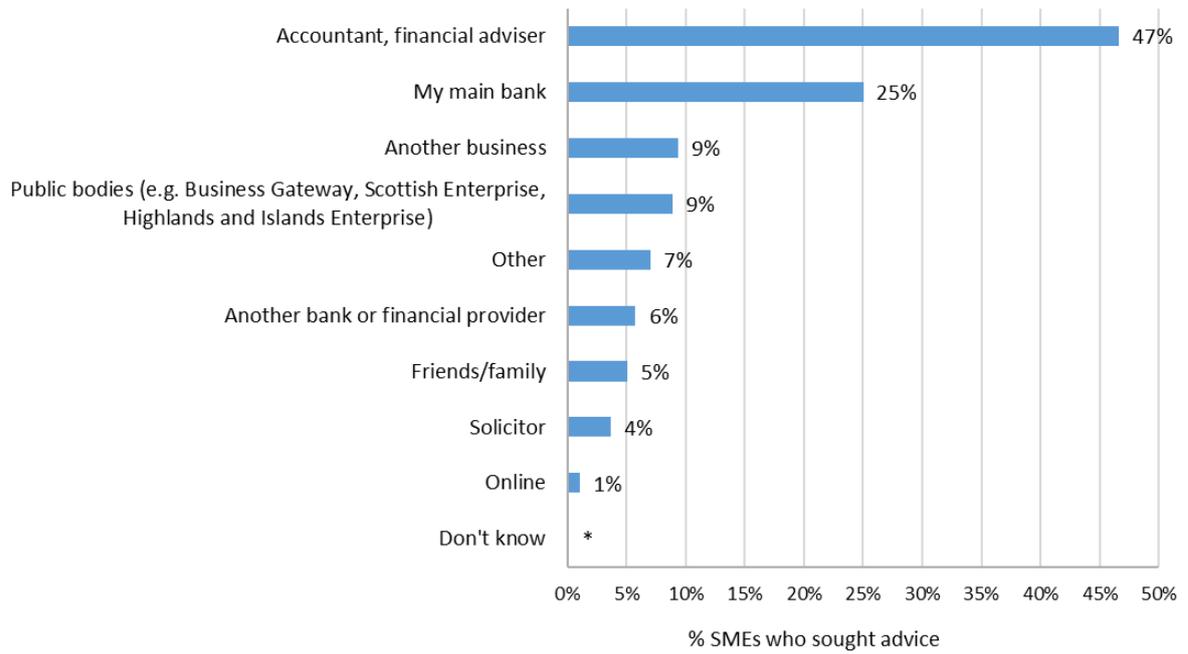
¹⁰⁰ The proportion of micro and small firms seeking advice was broadly in line with the all-firm average.

¹⁰¹ The sample sizes for this question are too low to allow for disaggregation by business type or sector.

Figure 28: Sources of external advice

Base: SMEs who sought external advice, 212

Multiple answers allowed across this question.



9. Obstacles facing SMEs

Summary

- When considered alongside other factors affecting business, access to finance does not appear to present a pressing problem to SMEs as a whole. However, when considering finance in isolation, a quarter of SMEs considered it to be a problem rated 5 or more on a 1-10 scale, where a higher score indicates increasing severity.
- Looking more granularly, more than one in ten medium-sized and manufacturing businesses rated finance as a critical problem, reflecting their higher rejection rates and indicating there were still groups of firms that faced issues in accessing the finance they needed.
- Local bank branches were considered more important by rural and agriculture SMEs and a higher proportion of rural SMEs felt bank branch closures were affecting their ability to access finance. This reflects the high value rural SMEs place on face to face transactions and the challenges some rural SMEs face in engaging with online banking.
- The ways in which SMEs felt bank branch closures affected their business differed to some extent for urban and rural firms however difficulties in depositing cash and obtaining tailored financial advice were common to both.

This section considers the extent to which SMEs consider access to finance and other issues, including bank branch closures, to present a problem for their business. The results are presented for SMEs as a whole and, where possible, for key sub-groups of interest including size band, sector, business type (high growth/exporter/new start) and location (urban/rural).

9.1 Access to finance

When considered alongside other factors affecting business, access to finance does not appear to present a pressing problem to SMEs as a whole. However, when considering finance in isolation, a quarter of SMEs considered it to be a problem rated 5 or more on a 1-10 scale, where a higher score indicates increasing severity. Looking more granularly, more than one in ten medium-sized and manufacturing businesses rated finance as a critical problem, reflecting their higher rejection rates and indicating there were still groups of firms that faced issues in accessing the finance they needed.

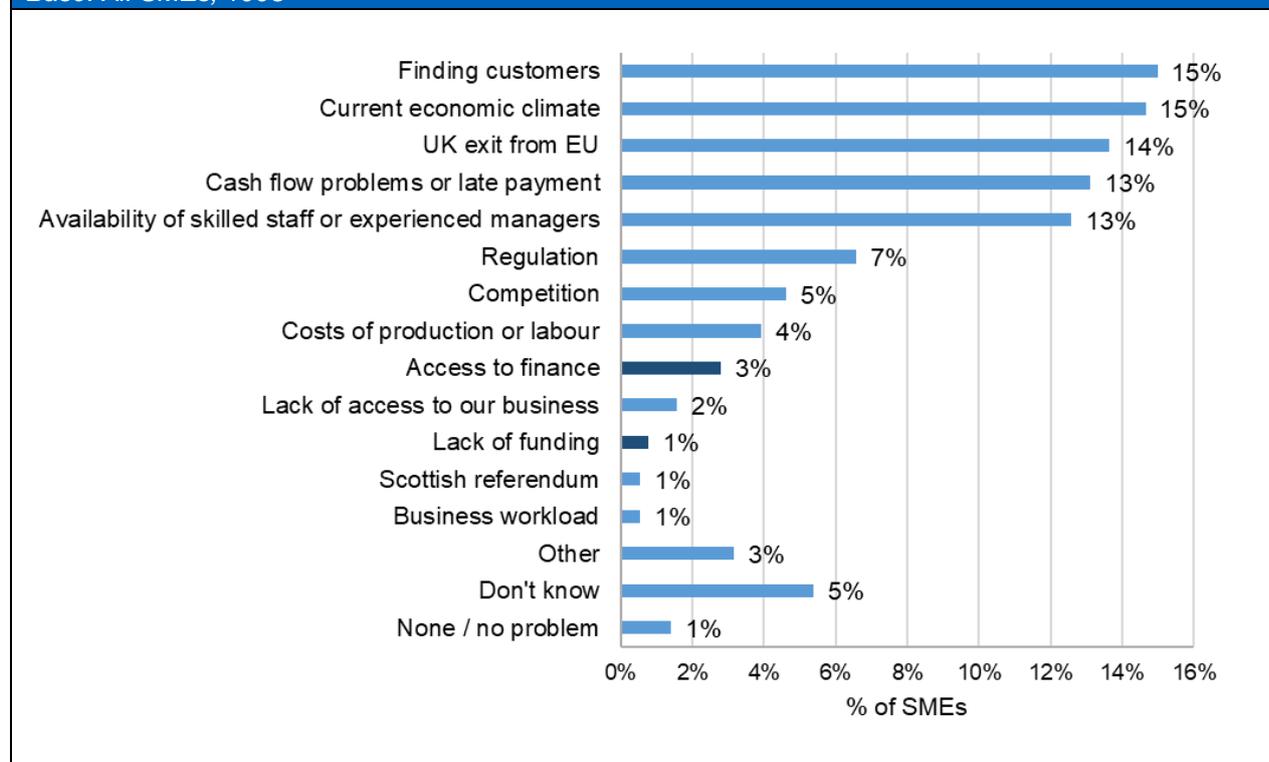
SMEs were asked what the most pressing problem currently facing their business was (Figure 29). The most commonly cited problems were finding customers, the current economic climate, UK exit from the EU, cash flow problems/late payment and availability of skilled or experienced managers. Access to finance was cited as the most pressing problem by three per cent of businesses surveyed. A lack of funding was cited by a further one per cent.

The results by business size band, business type (high growth, exporter and new starts) and location (urban/rural) were all in line with the all firm average. Looking at the sectors, a higher proportion of businesses in the 'other services' sector (6 per

cent) rated access to finance as the most pressing problem for their business. For all other sectors, the proportion was broadly in line with the all firm average.

Figure 29: Most pressing problem facing the business

Base: All SMEs, 1003



Businesses were also asked the extent to which obtaining finance and the cost of finance presented a problem to their business on a scale of 1-10 where 1 was no problem and 10 was a critical problem (Table 4). Almost half of all SMEs surveyed said finance presented no problem and only two per cent said it was a critical problem. However, around a quarter (27 per cent) of businesses rated obtaining finance and the cost of finance as '5 or more' on the 1-10 scale.

Table 4: Extent to which obtaining finance and the cost of finance presents a problem to the business

Base: All SMEs, 1003

Scale rating (1-10)	Percentage of SMEs
1 - no problem	49%
2	9%
3	5%
4	7%
5	14%
6	2%
7	4%
8	4%
9	2%
10 - critical problem	2%
Don't know	2%

Whilst just two per cent of SMEs overall rated finance as a critical problem, the results differed somewhat by business size, sector and firm type¹⁰². A higher proportion of medium-sized businesses (15 per cent), manufacturing businesses (13 per cent) and exporters (4 per cent) reported obtaining finance and the cost of finance as a critical problem, reflecting the higher rejection rates of these firms outlined in chapter 7, and indicating there were still groups of firms that face issues in accessing the finance they need. For all the other business sizes, sectors and firm types, the results were broadly in line with the all-firm average.

9.2 Bank branch closures

Given the shift to online banking and the number of bank branch closures in recent years, a number of new questions were added to the 2019 survey to understand the importance of local branches to SMEs and to consider whether, and in what way, the closures were affecting them.

Local bank branches were considered more important by rural and agriculture SMEs

The availability of a local bank branch was cited as important (very important or quite important) by over two thirds of all SMEs surveyed (68 per cent). Availability was perceived as more important to rural SMEs (77 per cent) compared to the average for all SMEs (Figure 30). This reflects findings from 2018 research undertaken by Highlands and Islands Enterprise¹⁰³ which highlighted the value that rural SMEs place on face-to-face transactions as well as the challenges that some rural SMEs face with broadband access and connectivity and their capacity and willingness to engage with online banking.

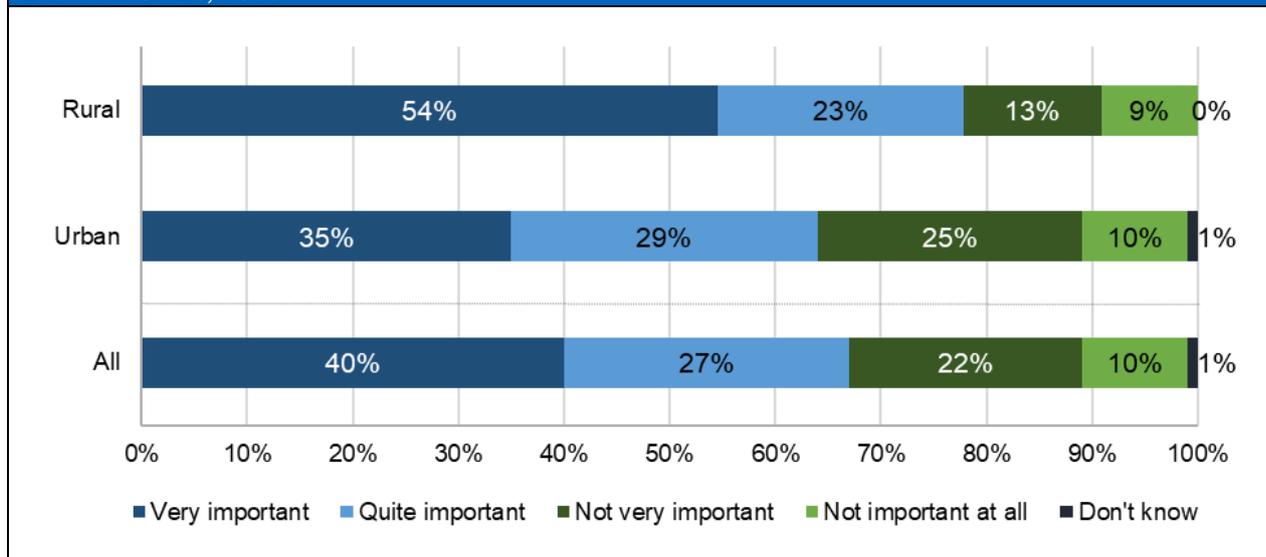
A lower proportion of small (51 per cent) and medium-sized (50 per cent) businesses cited local bank branches as important when compared to SMEs as a whole. Compared to the average for all SMEs, a lower proportion of exporters and new starts perceived local bank branches as important (51 per cent of each). Considering findings by sector, a higher proportion of SMEs in the agriculture (90 per cent), wholesale/retail (80 per cent) and other services (74 per cent) sectors considered bank branches to be important when compared for the all-sector average. Conversely, a lower proportion of SMEs in the business activities sector (44 per cent) considered them to be important compared to the all-sector average.

¹⁰² The results by location (urban/rural) were both in line with the all firm average.

¹⁰³ Highlands and Islands Enterprise, 2018, [Access to Banking Services in Rural Areas](#).

Figure 30: Importance of local bank branch to the business, by location

Base: All SMEs, 1003

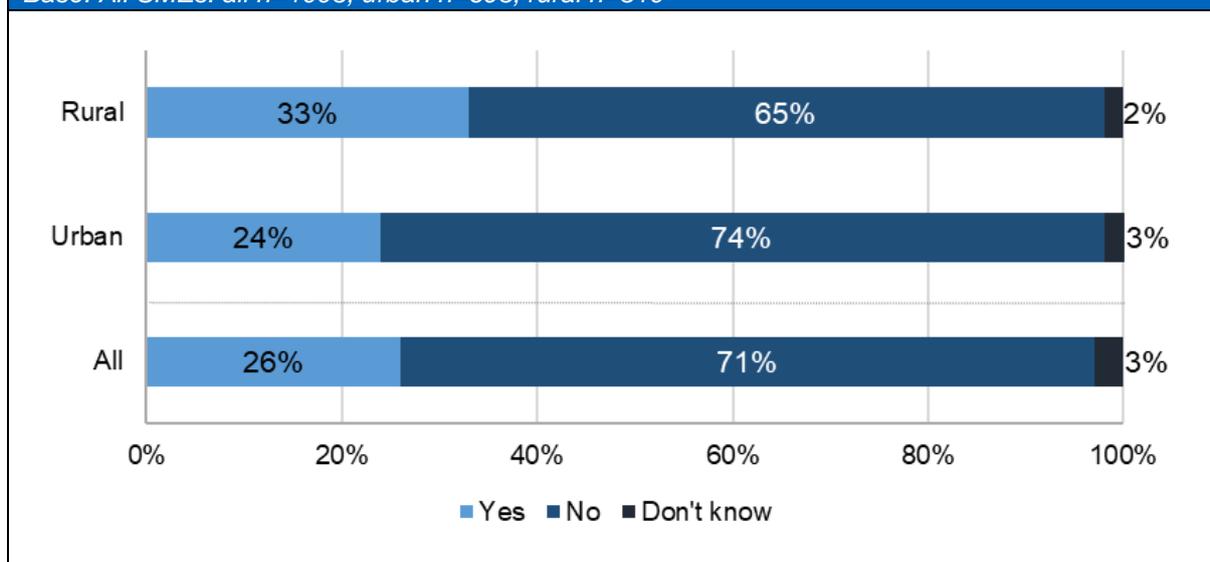


A higher proportion of rural SMEs felt bank branch closures were affecting their ability to access finance

A quarter (26 per cent) of SMEs surveyed felt bank branch closures were affecting their business' ability to access finance (Figure 31). Compared to the all-firm average, a higher proportion of rural businesses (33 per cent) felt branch closures were affecting them. Conversely, a lower proportion of small (19 per cent) and medium-sized (1 per cent) businesses and exporters (17 per cent) felt branch closures were affecting them¹⁰⁴. The results by sector were all broadly in line with the all-firm average.

Figure 31: Whether bank branch closures were affecting businesses' ability to access finance

Base: All SMEs: all n=1003; urban n=693; rural n=310



¹⁰⁴ The results for new starts and high growth firms were broadly in line with the all firm average.

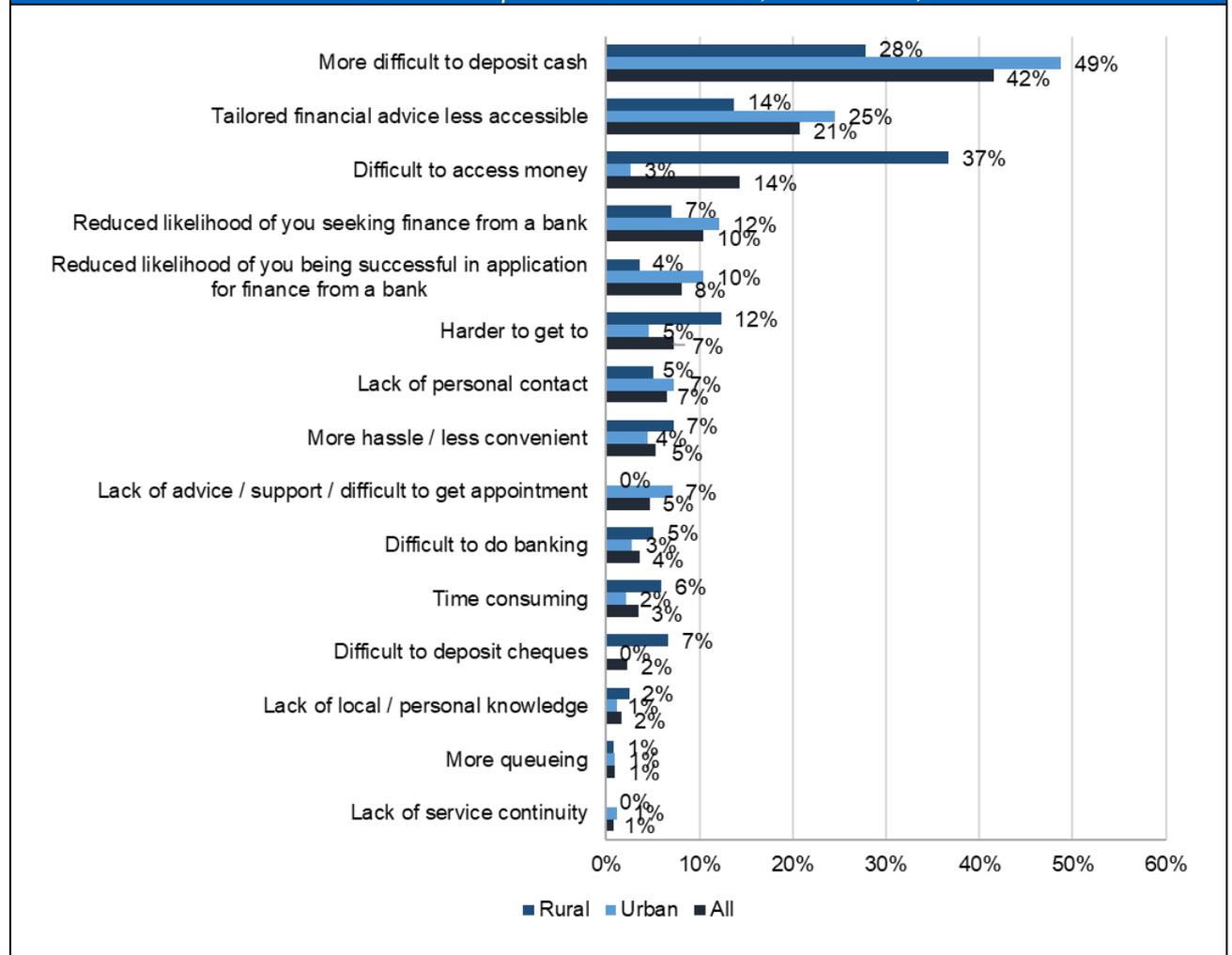
The ways in which SMEs felt bank branch closures affected their business differed to some extent for urban and rural firms however difficulties in depositing cash and obtaining tailored financial advice were common to both

SMEs who stated bank branch closures were affecting their business' ability to access finance were asked the ways in which this was happening (Figure 32). For SMEs as a whole, the most commonly reported answer was 'more difficult to deposit cash' followed by 'tailored financial advice less accessible'.

The ways in which SMEs feel bank branch closures have affected their business differed to some extent by location. Whereas 'difficult to access money' was the most commonly reported answer by rural firms (37 per cent), it was only cited as an issue for three per cent of urban firms. However 'made it more difficult to deposit cash' and 'meant tailored financial advice was less accessible' featured in the top three issues for both urban and rural firms¹⁰⁵.

Figure 32: Ways in which bank branch closures are affecting businesses' ability to access finance, by location

Base: All who think bank closures have impacted them: All n=261; urban n=171; rural n=90



¹⁰⁵ The sample sizes are too small to allow sectoral or firm size analysis for this question.



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