

# **SME OPPORTUNITIES FOR CHALLENGER BANKS**

The impact of Open Banking and changing attitudes among the UK's small and medium-sized enterprises

### **About the survey**

- The respondents to our survey come from all over the UK.
- They represent a range of industries, including manufacturing, construction, retail, hospitality and technology.
- Their businesses vary in age from under one year to more than 35.
- Most respondents work at small firms: 91% have fewer than 50 employees, and the remaining 9% have fewer than 250 employees.
- This is reflected in their relatively low turnover – 68% of companies bring in under £1 million a year (net), and just 5% turn over more than £10 million annually.
- Most (85%) have fewer than six people working in the finance department.
- Collectively, the needs of SMEs vary extensively.
- All figures, unless otherwise stated, are from YouGov Plc. Total sample size was 508 financial decision makers, of which 459 were from SME businesses. Fieldwork was undertaken between 7th – 13th March 2019. The survey was carried out online.



# This report explores the needs of UK small and medium-sized enterprises (SMEs) in terms of attitudes, goals and banking habits, and highlights opportunities for challenger banks.

In spring 2019, Finastra worked with YouGov to survey more than 450 financial decision makers from SMEs across the UK, gathering insight on this vast segment of the UK business market.

There are 5.7 million SMEs in the UK, making up 99% of businesses across the country.

### **Challenger bank opportunity**

Thanks to their size, lack of technical debt and digital-first approach, challenger banks believe they can outmaneuver established high street banks. Their agility helps them provide fast, reliable, seamless services to both consumers and businesses. And because challengers don't have the legacy of a large branch network, thousands of staff, and hard-to-replace technology, they have the potential to do all this at a lower cost.

These banks have only started to come to market in the past decade, and many of the front runners specialized in mortgages, meaning penetration among businesses remains limited. Addressing the broader banking needs of SMEs requires a correspondingly broad range of services – something that only a few challengers have recently sought to develop.

Challengers must persuade financial decision makers in SMEs that they are as trustworthy as established banks and can offer service that's at least as good. For example, while banking services for consumers, such as current and savings accounts, are free, business banking typically attracts charges. SME banks can incentivize switching by offering charge-free accounts for businesses.

SMEs are no strangers to innovation in banking. Card payments are now commonplace for businesses that for many years prioritized cash. The efficiency of new payment systems is winning out over the cost of cashing up and taking money to the bank each day.



# Are SMEs happy with their banks?

We were interested to see who SMEs bank with, how happy they were, and what services they value – now and in the future.



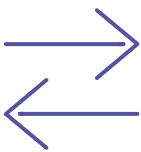
**88%**

of financial decision makers we surveyed say that their business holds its main account with an established high street bank.



**86%**

said they were either very happy or fairly happy.



**29%**

said that their business would be likely to switch its main bank account in the next five years – that is, before March 2024.

### Business as usual?

Perhaps unsurprisingly, 88% of financial decision makers we surveyed say that their business holds its main account with an established high street bank. Across the board, respondents were satisfied with the service they currently get from their bank. Around 86% said they were either very happy or fairly happy with the service received.

As to what financial decision makers value from their bank, fast payment processing came out on top, in importance for 95% of respondents. Next came a good mobile and online experience at 90%, followed by the availability to speak to someone to discuss specific business needs at 68%.

### Almost 3 in 10 looking elsewhere

While a huge majority of financial decision makers in SMEs seem happy with their banks, a large proportion would consider moving. Twenty-nine percent said that their business would be likely to switch its main bank account in the next five years – that is, before March 2024.

There is an opportunity here for challenger banks to attract these unsatisfied customers. Even if, as our research indicates, just 12% of financial decision makers in SMEs are unhappy, the size of the SME market in the UK is enormous and represents a huge addressable market. A House of Commons briefing paper from December 2018 estimates that there are 5.7 million SMEs (defined as firms with fewer than 250 employees), making up 99% of the number of businesses across the country. Combined annual turnover for SMEs in 2018 was £2 trillion, representing 52% of all private sector turnover.

In the next three chapters, we dig deeper to find out more about the SMEs that challenger banks should be targeting.

# Rise of the millennial finance managers

**A significant portion of our respondents could be considered millennials or near-millennials: 20% were born after 1975.**

**Respondents under 45 years of age are more prepared to switch banks, with 49% saying that their business would be likely to switch its main bank account in the next 5 years.**

While most sources give the start of the millennial generation as being the early 1980s, many commentators have identified a crossover between Generation X and Generation Y in the late 1970s and early 1980s.

That so many millennials should figure in a survey of financial decision makers is hardly surprising. A PwC report predicts that this generation will comprise 50% of the workforce by 2020.

### **Digital is key for this growing demographic**

Firstly, banks need to work hard to build loyalty with these customers. Respondents under 45 years of age are more prepared to switch banks, with 49% saying that their business would be very or fairly likely to switch in the next 5 years compared to 29% overall.

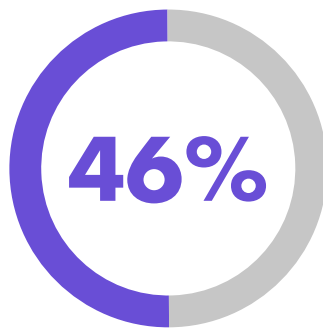
Secondly, a good mobile and digital experience is a must: 94% of them said it was important vs. 86% of over 55s. To substantiate key reasons for switching business bank accounts overall, those that had done so were motivated by a better digital or mobile banking service in 9% of cases. And 40% of under 45s would consider banking for their business with a digital giant like Google, Amazon, Facebook or Apple (GAFA), should these companies enter the market. In contrast, only 13% of 55 and overs feel the same way.

Young financial decision makers' preference for the streamlined digital experience that new banks have mastered, as well as their willingness to explore new banking options, is good news for challengers. However, they still have a significant amount of work to do: 80% of younger financial decision makers in SMEs say they are happy with their main bank.

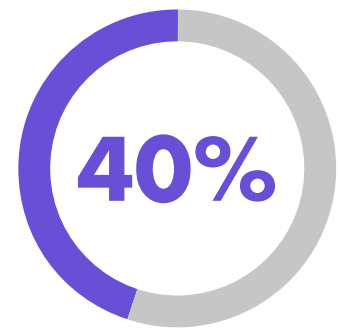
### **New companies, new attitudes, new bank**

Company age, too, was an interesting indicator. Forty-six percent of financial decision makers in companies formed within the last five years said they are likely to switch their business' main bank account before 2024. And these newer companies are more likely to seek out new forms of banking: only 78% of financial decision makers in this category said their their company use high-street banks (down from 88% overall). These companies also had slightly more under 45s in positions of financial responsibility: 36% as opposed to 20% across businesses of all ages.

It is not unreasonable to think that younger firms with no legacy – regardless of the business founders or people working there – would consider a fresh approach to business banking. SMEs established a decade or more ago would have almost certainly gone with a major high street institution, which gives challengers the additional obstacle of forcing a change in supplier. Challenger banks would do well to consider targeting potential business founders before they even form their companies, perhaps by working with universities or startup incubators.



**of SME financial decision makers in companies aged under 5 years, said that their business would be likely to switch its main bank account in the next 5 years, compared to 29% overall**



**of under 45s would consider banking with a digital giant like Google, Amazon, Facebook or Apple (GAFA), should these companies enter the market**

# Meet the switchers

**We've discovered how many SMEs are likely to switch their main bank account in the future, but 42% of respondents say their business has already done so in the past.**

**Recent switchers are more likely to cite a better digital or mobile service as a reason to switch.**

Forty-one percent of financial decision makers in SMEs also say that their business has previously opened a new account with a secondary bank. The reasons for switching reflect the value placed on certain services, as detailed on page 5. Of the SMEs that have switched and opened an account with a new bank, 29% said that this was because the new bank(s) offered better overall service. While 26% of financial decision makers said that their business had moved because it was unhappy, 19% said that their business had received an incentive to move, but only 9% moved because of a more compelling mobile or digital banking service.

Of the 12% of respondents who said they were unhappy with their bank, the top reason was poor customer service at 46%, with high banking charges not far behind at 43%. This was followed by failing to understand the needs of a customer's business at 28%. Only 9% said that their bank lacked the online services their business needs. This may serve as a wake-up call to some challengers that pride themselves on offering a no-frills, digital-only service. Differentiation beyond the online experience is important too.

### **Recent switchers could be your dream customer**

In our data, we found a subset of switcher decision makers that challenger banks will want to know more about: 23% of all financial decision makers said that their SME business had begun business with a new bank in the past three years. These recent switchers show a preference for digital-first services.

Like the SMEs with millennial decision makers, recent switchers are more likely to cite a better digital or mobile service as a reason to switch (17% vs. 9% for all respondents). And they are more open to using banking services from the GAFA companies that have made a seamless online and mobile experience their bread and butter. Overall, 22% of respondents said they would consider banking with a GAFA company for their business, while 40% of recent switchers would be open to it.

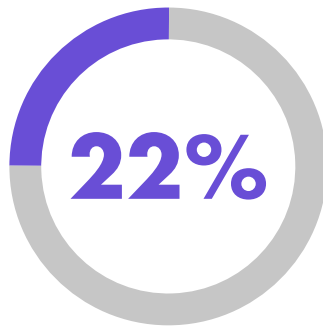


### Winning a switcher is just the start – keeping a switcher is the hardest part

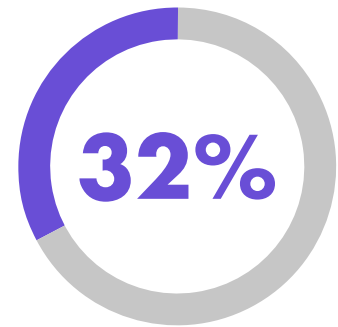
We also found some interesting results when we looked at the banks that SMEs had switched from and to. On the one hand, companies are indeed (slowly) moving from traditional banks to both new high street banks (like Metro) and online banks (like Monzo). Close to one third (32%) of recent switchers now hold their main account with challengers. But it's not all one-way traffic. Fifty-three percent of SME financial decision makers whose business were using a new bank in the last 3 years said that their business was likely to switch again in the next 5 years.

This data indicates that switchers are prepared to look for the best service and value. While challengers might see this segment as readily primed for their innovative services, they should be cautious. Switchers know how easy it is to change banks and show a propensity to do so again. Challengers must be aware of this and work hard to retain these customers. Challengers must rapidly innovate to continually evolve their offering to these hard-won customers.

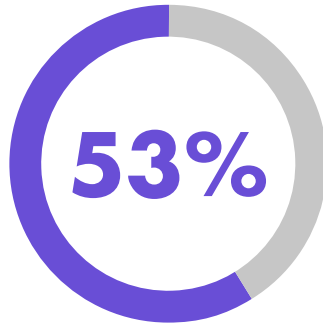
They will also need to appeal to the many sub-segments of the SME market. For example, multi-currency offerings are vital for businesses where employees travel frequently, or where import and export make up a large proportion of activity.



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# The opportunity of Open Banking

**Those of us working in the finance sector will be more than familiar with Open Banking, but it's not a topic that's made it into the public conscience.**

Just 11% of our respondents had heard of the term Open Banking, although that rose to 17% for under 45s and 24% for firms that had begun business with a new bank in the last 3 years.

Nor does it seem to have much penetration with UK SMEs. Open Banking was introduced, in part, to improve competition in financial services for the benefit of banking customers, including SMEs. In time, Open Banking will see SMEs being offered a wider variety of more appropriate services. That said, just 11% of our financial decision makers in SMEs had heard of the term, although that rose to 17% for under 45s and 24% for financial decision makers in firms that had begun business with a new bank in the last 3 years.

### Open what?

While most don't know what Open Banking is, many value the opportunities it presents. Twenty-four percent would like to see bank data synced to accounting systems for easier tax returns, and 19% saw the appeal of automating their invoicing and/or payables processes.

As digital banks evolve, they will benefit from providing a wider portfolio of services. In many cases, they will focus on very specific products and niches, including payment services, SME lending, peer-to-peer lending, working capital loans, payroll, business insurance services and trade finance. However, some 39% of SME financial decision makers said they weren't interested in any of the proposed benefits of Open Banking, suggesting more education around the potential benefits of new Open Banking services is needed.

### SMEs not ready for data sharing

Open Banking requires customers to opt in to giving third parties access to their data. SMEs overall are reluctant to do this. Sixty-three percent of financial decision makers in SMEs are uncomfortable with the idea of sharing their company's data so that third parties can offer additional products relevant to their business. Twenty-seven percent felt comfortable doing so.

Again, younger people and recent switchers were more willing to benefit from additional new services as a result of sharing data. Forty-four percent of under 45s were comfortable with the idea, as were 43% of companies who had opened a new bank account with a new bank or switched main account to a new bank in the last 3 years.

There is clearly an appetite for the services enabled by Open Banking. Challengers naturally tend to be customer centric. That said, they will have to work hard to understand and then meet the financial needs of such a broad range of customers. Central to this is educating all SME customers about the benefit and relevance of these Open Banking-enabled services.



# Positive momentum for challengers

**While most SMEs are content to stay with their banks, a significant portion would consider moving.**

**There is an opportunity to better serve the most forward-thinking financial decision makers.**

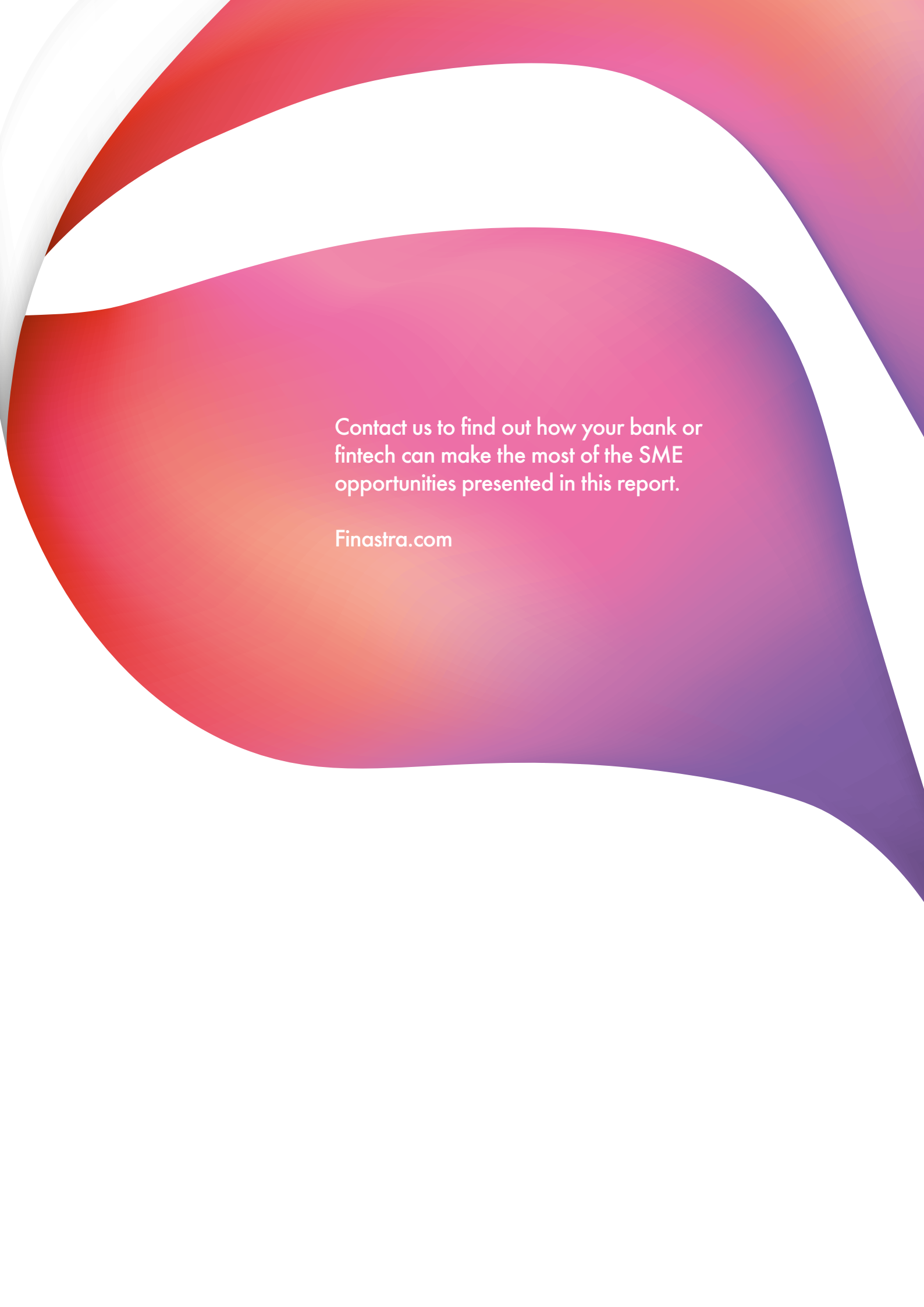
Young people that are taking up positions of financial responsibility within SMEs are more open to banking with challengers than their older peers. Newer SMEs are also emerging as a key market.

Established banks have managed to hold on to most of their customers, but inertia plays a big role. Businesses that have recently switched show that they are more aware of modern banking trends and opportunities – and awareness of new ways of banking is only going to grow. These companies represent an ideal audience for challengers – but expect to work hard to win their loyalty. To win, banks need to rapidly evolve their portfolio of SME banking services and to build their ecosystem on a retail banking platform that allows them to scale rapidly.

As well as persuading SMEs to switch their main accounts, it is worth communicating the value of other products. Many customers are open to multi-banking and taking new financial products from new providers.

This enables challengers to build trust and loyalty. Nineteen percent of firms that opened an account with a bank other than its main bank did so by opening a secondary account. This may be an easier route for SMEs, which don't have to worry about severing ties with their old bank. But it remains to be seen whether SMEs remain loyal to new digital providers.

While Open Banking is still not fully adopted or understood by SMEs, there is an opportunity to better serve the most forward-thinking financial decision makers, thanks to the new services that Open Banking enables. Challengers and fintechs can position themselves as innovators by promoting the benefits of a wider portfolio of digitally enabled financial products. Challengers also have the opportunity to educate potential customers about how to take advantage of these digital products.



Contact us to find out how your bank or  
fintech can make the most of the SME  
opportunities presented in this report.

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## About Finastra

Finastra unlocks the potential of people and businesses in finance, creating a platform for open innovation. Formed in 2017 by the combination of Misys and D+H, we provide the broadest portfolio of financial services software in the world today—spanning retail banking, transaction banking, lending, and treasury and capital markets. Our solutions enable customers to deploy mission critical technology on premises or in the cloud. Our scale and geographical reach means that we can serve customers effectively, regardless of their size or geographic location—from global financial institutions, to community banks and credit unions. Through our open, secure and reliable solutions, customers are empowered to accelerate growth, optimize cost, mitigate risk and continually evolve to meet the changing needs of their customers. 90 of the world's top 100 banks use Finastra technology. Please visit [finastra.com](https://finastra.com)

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