

Can the UK finally crack a problem hindering SMEs?

The financial services industry has traditionally found it very difficult to serve the disparate and fragmented SME marketplace. But we believe that the combination of traditional financial providers and new entrants focused on data and analytics means that SMEs will finally get the financial services they deserve.

Confronting this challenge is crucial. Prior to the COVID-19 pandemic, which has itself underlined just how challenging it can be to design one-stop-shop solutions for very different businesses, there were around 5.9M small and medium-sized enterprises active in the UK according to official data.

Collectively, these businesses accounted for close to two-thirds of employment in the private sector and generated just over half of all private sector turnover. All these SMEs need access to financial services, from banking facilities to financing and insurance. Yet the established financial services industry has often found it tough to meet these needs.

Too big to ignore, too small to serve

The Bank of England suggests, for example, that SMEs in the UK are suffering from a £22B funding gap; other studies have highlighted similar shortfalls in other areas.

There are good reasons for this. For large, vertically-integrated financial services providers such as banks, SMEs are collectively too big to ignore, but individually often too small to serve. In a marketplace lacking homogeneity, no two SMEs are the same, the complexities of segmentation and bespoke service provision make for high costs; the value generated by each SME, meanwhile, is limited.

Finally, however, we are on the cusp of overcoming these problems, courtesy of two significant evolutions in the financial services ecosystem.

First, we are seeing innovative new entrants to financial services, leveraging technologies such as automation and data analytics to make decisions in areas of the SME market where incumbent providers have found the going tough.

And second, a combination of Open Banking reforms introduced at the beginning of 2018 and the accessibility of data in cloud accounting software, are slowly but surely ensuring these fintechs can access the data they need to fuel their technology engines.

Both these drivers are vital. Analytics tools and automation technologies enable fintechs to segment the market, mechanise decision-making and deliver bespoke products and services. This reduces their cost to serve and increases the value that each SME client generates.

Without access to good data, however, these tools will come up short. Open Banking and cloud accounting ensures this access, enabling new entrants to unlock the information and insight that for years has been stuck in banks' functional siloes.

We are in the relatively early days of the Open Banking revolution, but as access to data accelerates, the ability of fintechs to serve SME customers will increase exponentially.

Unlocking SMEs' growth potential

We are already seeing many good examples of what is possible. Gresham House investee company Funding Xchange has built a platform which automates the decisioning around lending to SMEs, providing businesses seeking finance with a single point of access to more than 40 lenders; it promises personalised quotes within four minutes and finance that is available

within ten minutes.

Rainbird, another investee business, is pioneering the use of intelligent automation tools in financial services companies (and in other sectors) to speed up decision-making and improve customer outcomes.

Also, Equipsme has developed a product which makes health insurance accessible to SMEs, with coverage starting from as low as £7 per person per month and a greatly simplified application process – with no medical pre-screening required.

Interestingly, all these businesses have been quick to step up to the challenges posed by COVID-19. Funding Xchange has established itself as a crucial hub, enabling SMEs to assess and access the various government loan schemes launched in response to the crisis.

Rainbird is making its technology available for free to automate complex decisioning where that helps overcome the disruption that the pandemic is causing. Equipsme is providing its services free of charge to SMEs with 2 to 20 employees until 1 August.

Working together, not in opposition

Importantly, the businesses emerging in this space do not typically regard themselves as replacing incumbent providers. Rather, their business models are built on collaboration as opposed to competition.

This makes sense. Many large banks and financial institutions freely acknowledge that their size and structure prevents them from serving SMEs as effectively and efficiently as they would like.

Partnerships with emerging fintechs represent an opportunity to resolve this problem, to the benefit of all concerned – including SMEs themselves. There are also benefits for the fintech companies, as they can make use of established distribution channels and limiting acquisition costs which can burn significant cash.

As a result of that, we are most excited about scaling businesses in the financial services sector which are focused on helping the banks themselves through the digital transformation process, rather than working directly with customers such as SMEs.

The importance of these fintechs should not be overlooked; they will play a vital role in ensuring that in future, banks too can better service the SME audience.

At this time of heightened concern about the financial services sector's ability to serve SMEs, there is every reason to be hopeful.

A community that has, even before the COVID-19 crisis, been overlooked by the financial services sector, is now securing access to a much broader and deeper range of solutions. And leaving the immediate threat of the pandemic aside, the long-term potential of this evolution is hugely exciting.

Fintechs and other new entrants are set to provide SMEs with the products and services they need to power sustained growth.

Henry joined [Gresham House](#) in November 2018 and focuses on growth capital investments into software and service businesses in the financial and professional services sectors, with a particular interest in process and workflow automation software, service companies looking to drive digital transformation, scale-ups looking to improve the use of data and analytics for large incumbents, and new methods of communication and collaboration.

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