31 July 2016

**SME remedies**

I am responding to your recent report on retail banking and specifically the part about proposed remedies for SMEs.

I have been the Independent External Reviewer to the banks SME Appeals Process since its inception in April 2011 and over the last 5 years. In that period since then there have been almost 16,000 appeals and of those around 30% have been overturned. The examination of these appeals has allowed me to build up one of the largest and most exact data bases on SME lending in the UK and I report Annually on issues publicly as well as meet regularly with HMT on issues arising from that, plus with the individual banks to recommend process changes to the way they lend to SMEs which have all been implemented over the last 5 years so the ways banks and SMEs inter relate is now much better than it was then which is one of the main successes of the Appeals Process.

Prior to this role I was Chair of the CBI's UK SME Council so over the years have built up a large personal knowledge based on evidence on how both SMEs and banks operate.

The specific part of your report that concerns me in that it will probably worsen the situation between both those parties is set out below.

***Retail banking market investigation***

*Provisional decision on remedies*

*We have provisionally decided to make an order requiring all lenders that provide unsecured loans and overdrafts to SMEs to display on their websites rates showing the cost of these products up to the value of £25,000. These rates must be displayed in a form used under the existing (personal) consumer credit regime. This includes:*

*(a) showing a representative annual percentage rate (APR) for unsecured loans; and*

*(b) an equivalent annual rate (EAR) for overdrafts to enable SMEs to make comparisons on the total cost of credit.*

*The rates that these lenders publish must be made available to at least 51% of SME customers applying for these products. In addition, lenders must make available these charges, terms and conditions, and how APR/EARs vary with loan size and length, as open data to third parties, such as comparison sites and finance platforms, including the eventual Nesta challenge prize winner or winners. This measure must be implemented within three months of the order coming into effect. We further require that all lenders who advertise prices for SME lending in marketing materials should always do so using an APR/EAR format from the existing (personal) consumer credit regime.*

*We have also provisionally decided to make an Order requiring RBSG, LBG, Barclays, HSBCG, Santander, Danske, BoI and AIBG to offer a tool on their websites to enable SMEs to obtain an indicative price quote and indication of their eligibility. This would cover all unsecured and secured loans and overdrafts up to £25,000. This measure must be implemented within six months of the order coming into effect. Access to these tools must be made available to any two finance platforms designated under the SBEE Act for a period of three years and any two comparison sites, including the eventual winner or winners of the Nesta challenge prize, for a period of three years after the prize winners have launched their products in the market.*

I do understand that the above and indeed the whole of the CMA report are only for now 'provisional remedies' and have asked for comment from the banks and others but I do have a concern. My concern is in the final paragraph of the above and relates to the CMA's desire to want each of the banks listed to have in place an on line tool so that SMEs can get both a price quote but also their eligibility to be accepted for lending for the amount they are looking for and it is the last part of that that concerns me. The reason it concerns me is that anything that we do to help customers and banks should make that interaction and relationship between them better not worse and I am concerned that this suggestion would have the opposite effect.

That the banks could produce a tool that could make that judgement is not in doubt. I have witnessed banks using or experimenting with both simple and sophisticated tools that can do that and do it well if the information that is inputted into it is accurate and therein lies the challenge I believe.

Over the last 5 years I have listened and watched many lending conversations between lenders and small SMEs which are those that are most likely to apply for less that £25,000 lending. As I have said many times in these reports the sophistication in terms of financial knowledge tends to relate to how large the SME is and in this area they will tend to be small so less sophisticated in general. To obtain a sensible solution to eligibility the customer will have to provide turnover or revenue figure, costs, net profit etc. From my experience what small SMEs tend to answer to those questions varies greatly and not always correct for a variety of reasons usually to do with what they think is revenue, what they differentiate between personal and business costs, and what net profit means. Now while the banks could make definitions of what they mean by each on their website experience makes me concerned that SMEs will still enter incorrect data which could give the wrong answer in terms of eligibility either way.

Lack of financial and business knowledge has always been an issue with micro and small SMEs and still is and I see many times small SMEs being declined and then overturned because correct information has not been submitted initially.

It is well known that there is a lot of education that needs to be done with small SMEs and the debate has always been who should do that and I recall when I was Chair of the CBI's UK SME Council some years ago us discussing that, with no solution, many times. While I accept that these recommendations to the CMA may have come from the Trade Associations, who have micro and small SMEs as members, with the best intentions they might give the opposite result than was desired.

What is meant by eligibility in the paragraph in the CMA report also needs defining as it could mean different things and also would have to be heavily caveated until full due diligence was done by the lender on any application.

I am all for putting new tools in place but only if they add value and make the relationship better and I am not sure that will be the case with this. I intend to write to the CMA in those terms.

The above will be published in my Annual Report which I will be releasing this week so would ask you to consider this as part of the input you asked for.

I am happy to discuss it with you.

Best wishes

Russel

Professor Russel Griggs OBE