Allica Response to CMA Consultation on Removing Bundling Requirement

We are strongly opposed to the removal of the Bundling Requirement, and set out the rationale for our position below.

The current bundling limitation already does allow designated banks to bundle in some situations, e.g.:

(a) where required for shared security (e.g. current account with an authorised overdraft limit that uses the same debenture mortgage security that is used for a business loan); or

(b) if there is a price incentive (i.e. the customer gets better fees/interest by taking the integrated product than not, subject to the customer being allowed to take the products separately if they wish).

Bundling practices that are essential for a loan or provide an advantage to the customer are therefore already permissible. Challenger banks, which aren't subject to this Restriction, operate in the market according to (a) or (b): we do not see examples of challenger banks just demanding that a business current account (BCA) is opened with every loan with no customer benefit. We would indeed be supportive of a position that no bank (not just the current designated ones) can bundle a business current account with a loan unless there is a customer benefit as per (a) and (b).

This supports our belief that eliminating the Restriction would only risk harming customers both for lending and BCAs.

Many of our leadership team have worked in senior roles in major banks (including in roles that included direct responsibility for Bundling compliance). The rule against bundling is deeply ingrained in the operational procedures and training of major banks and in the mindset of their SME employees, having been in effect for over two decades. Considering this, the potential advantage of removing the Restriction for these major banks appears minimal as it does not seem to impose any significant ongoing operational costs, which would be the only benefit of its removal.

We believe it is critical that the CMA carefully considers the relevant market here, rather than just looking at SME as one segment. There are crucial differences in the competitive position when looked at on a sub segmented basis.

SME Business Current Accounts (BCAs)

There is a major distinction to be made between micro SMEs (<5 FTE, typically 1 FTE) and established SMEs (>5 to 10 FTEs). Micro SMEs are very large by number being c.90% of businesses, however they have much less economic contribution being c.14% of GVA, while the 10% of businesses that are established SMEs represent c.35% of GVA. There has not been sufficient attention paid to the established SME market, which is critical to the UK's economic growth.

The new start and micro SME BCA market has changed a lot in the last decade (led by Tide, Starling and Monzo, supported by large Banking & Competition Remedies grants), with total market share of neobanks in microbusiness estimated at c.25% (and around half of the market for new starts).

However there has been no change in the established SME BCA market. Allica recently conducted a survey of established SMEs[1].

The survey showed the 5 major banks holding 89% established SME BCA share, other traditional banks 5%, and digital banks 6%. We would posit that this 89% share of the 5 major banks is unchanged, or possibly even more concentrated (given merger activity of challengers such as HBOS and Alliance & Leicester into LBG and Santander in the Global Financial Crisis) than when the limitation was introduced in 2002.

Well under 1% of new start micro businesses ever grow to become established SMEs, so it cannot be relied on that increased competition in micro SMEs will feed through in any near term period to established SMEs.

And there is very little competition in the bank switching market with Pay UK data showing there are only c.20-25k CASS switches p.a. for business/charities, which is less than c.1% of SMEs that could be switching (based on businesses >2 years old).

As a result the outcomes for customers are very poor.

Allica publishes research, supported by the FSB and IOD, research which shows that SMEs keeping around half of their cash balances on non interest bearing current accounts ('NIBCAs') is costing them up to £5.5bn per annum vs top quartile rates they could receive placing money on instant access accounts. There is a further £3bn in interest per annum being missed by SMEs keeping money on low earning instant access accounts at designated major banks, where there is a nearly 3% difference in the average interest rate being paid to SME vs a Corporate by major banks.

The situation was very different in the 2000s, where only 10-20% of SME cash was held in NIBCAs and the rest in interest earning accounts paying a competitive yield - SMEs got conditioned over the 2010's decade of near zero interest rates to not seek to look for yield on their cash. This SME inertia through NIBCAs is now providing a major funding cost advantage to the major banks for lending now interest rates have risen. For example, Cynergy Bank (a competitor to Allica in the established SME space, in both BCA and lending) in its recently published annual report says *"The current savings environment gives significant competitive advantage to the clearers and those organisations with a large current account base leading to significantly lower costs of funds"*

Given the still extremely concentrated nature of the established SME BCA market, and poor outcomes on SME deposit interest rates, we cannot see how removal of the Bundling Restriction would improve this situation and would likely embed it further.

SME Lending

The established SME market is critical in terms of the CMA considering the linkage between Loans and BCAs, as c.77% of SME lending goes to firms with 10+ employees.

[1] There were 205 respondents with 7% having 5-9 FTE, 43% 10-50 FTE, 25% 51-100 FTE, and 25% 101-250 FTE

Regarding loans, the most recent British Business Bank annual review indicates that 50-60% of SMEs[2] only consider a single lender, and SME Monitor data reveals that almost half (49%) go straight to their primary bank for borrowing.

So making a return to tied loan with BCA would likely enable the major banks to increase these percentages further, and seek to reduce broker share. The use of brokers for SME finance has grown very significantly since the 2002 order was introduced, and also significantly since the last CMA review in 2015/2016. Brokers are the main channel by which challenger and fintech SME lenders have grown their share of SME lending over the last decade.

Our leadership has worked at designated lenders including HSBC and Barclays, and from this experience there saw a general reluctance to work with the broker market and a strong preference for 'direct' relationships.

Brokers are crucial to fixing the problem of SME discovery and access to finance now there are a diverse range of SME lenders in the market (for example the Finance and Leasing Association has 150 lenders, and there are likely a further 50-100 further lenders on other SME lending products). Brokers are particularly important for SMEs of up to 50 FTE where often there is no full time FD/CFO (NACFB data shows the average broker SME loan was for a company with 16 FTE).

SME business owners are rarely financial experts and are time poor, so brokers are a vital aid to SMEs to navigate the now diverse SME finance market.

So to further improve access to finance in the SME segment and thereby productivity and growth, it is important that broker usage continues to grow from an estimated 25-50% of SME lending (varying by product) towards the residential mortgage market position of c.90%.

Permitting the tying of a loan and a BCA when there is no benefit to the customer cannot improve the SME lending market and could significantly hinder the growth of the broker channel and, thereby, access to SME lending itself.

[2] 51% in 2023, 58% in 2024