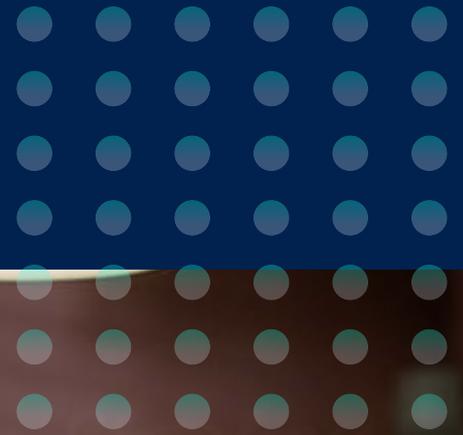


The Great British Savings Squeeze

A report into the state of the SME business savings market



GREAT BRITISH
SAVINGS SQUEEZE
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Introduction

Small and medium-sized enterprises (SMEs) are the engine room of our economy and a vital part of our communities.

Small firms (made up of those businesses with under 250 employees) employ 16.4 million people (60% of the UK workforce) and generate more than half of the country's GDP.

SMEs also have £273 billion of hard-earned money sitting in bank accounts. These savings have been a lifeline for many businesses who have seen their cashflow battered by a range of factors over the past decade, from the covid pandemic to Brexit and the cost-of-living crisis, where SMEs have often felt the economic crunch, harder and sharper than other larger companies.

With soaring inflation, rising costs, and ongoing economic and political uncertainty meaning more of this cash is being held back rather than invested, it's crucial that UK SMEs can get a good return on their hard-earned savings.

Since the Bank of England started increasing interest rates in December 2021, there has been significant attention given to the personal savings market. The pace at which these increases have been passed on by the banks to consumers has been under close scrutiny, in the hope that personal savers won't leave their savings to dwindle in zero or low interest accounts.

Allica has long thought there may be similar issues impacting SMEs – but to date there has been no real scrutiny of the business savings market.

Allica Bank's research explores the state of the UK business savings market to determine whether it's fit for purpose for SMEs, and whether they are getting a fair deal in comparison to their larger, corporate counterparts.

SMEs also have £273 billion of hard-earned money sitting in bank accounts.

¹ gov.uk, 'Business population estimates for the UK and regions 2022'

² See table 1

Key statistics

SMEs have **£273 billion** of cash on deposit.

£149 billion of this is sitting in current accounts, earning **ZERO interest**.

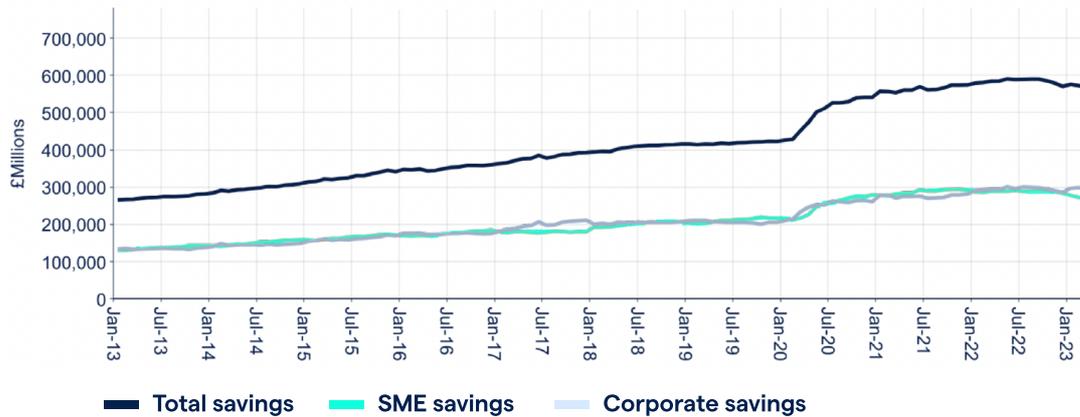
The remaining **£125 billion** is earning **2% less** than large, corporate firms.

SMEs are missing out on more than **£7.5 billion** in interest every year.

The size of the business savings market

Looking at data from a range of sources, including the Bank of England and UK Finance, we can see that the size of the business savings market is significant. Nearly £600 billion is currently kept in business savings accounts by both SMEs and corporate businesses.

Table 1 Savings market, by size of business



Source: Bank of England Bankstats (Sep 2023), UK Finance data (Q1 2023), Annual reports & websites of relevant financial institutions

The size of this market has doubled in the past ten years from £267 billion in January 2013 to £568 billion in March 2023. Throughout this period, the split between SME and corporate savings has remained roughly equal. In March 2023, SMEs were reported to have £273 billion on deposit, while corporate businesses had £295 billion.

Table 2 Savings market, by size of business

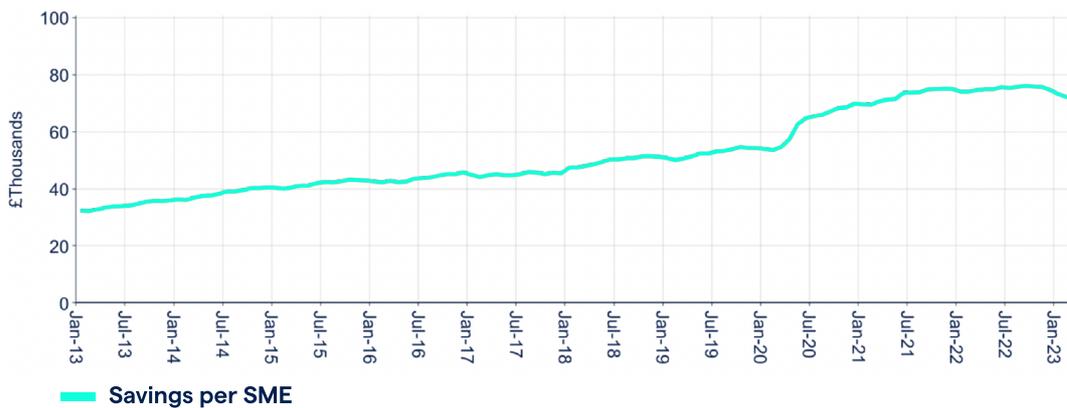


³ Source: Bank of England Bankstats (Sep 2023), UK Finance data (Q1 2023), Annual reports & websites of relevant financial institutions

How much savings do SMEs have?

By dividing the size of the SME savings market by the number of SMEs in the UK, we are able to calculate the average amount of surplus cash an SME in the UK has on deposit.

Table 3 Savings per SME



Source: UK Finance SME Aggregates data (Q1 2023), Annual reports & websites of relevant financial institutions

Between January 2013 and March 2023, that amount has more than doubled (+123%) from £32,400 to £72,210.

There was a notable uptick in the size of the SME savings market during the covid pandemic, which saw an increase of 30% between February 2020 (£53.7 billion) – one month before lockdown was introduced – and February 2021 (£69.6 billion). This compares to an increase of just 7% in the same period one year before (£50.2 billion in February 2019, rising to £53.7 billion in February 2020).

In other words, the average amount of savings an SME had in the UK the month before the pandemic lockdown was introduced in March 2020 was £54,680. One year later, in February 2021, that had risen to £69,580. It's clear that the uncertainty of that time meant businesses were feeling the need to keep more cash aside, typically by taking out a government guaranteed loan (e.g. a Bounce Back Loan).

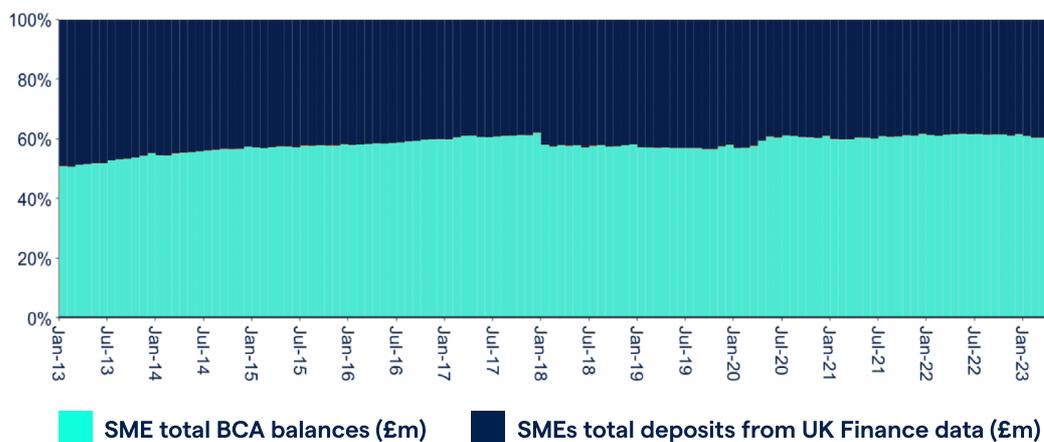
The post-pandemic savings bump peaked in September 2022 at £76.2 billion.

³ Total SME savings are calculated as the sum of SME Current A/C balances and SME Deposit data from UK Finance, and reported balance sheet data for Starling, Metro, Aldermore, Cambridge & Counties, and Handelsbanken; Corporate savings calculated as the difference between Total private non-financial corporation (PNFC) savings and SME savings

What interest are SMEs earning on their cash?

Next, we looked at how hard the surplus cash SMEs have on their balance sheet is working. Notably, the majority of SME deposits are being held in current accounts rather than savings accounts, where they're earning no interest at all. The proportion sitting in current accounts has risen steadily over the past decade from 50.8% in January 2013 (totalling £63.7 billion) to 60.4% in March 2023 (£149 billion).

Table 4 SME savings per composition



Source: UK Finance data (Q1 2023)⁴

The remaining £125 billion is kept in a mix of instant-access, notice and fixed-term savings accounts, which do earn interest. By taking the average interest rate offered to SMEs by the major business banking providers and weighting it by market share, we found that SMEs are earning an effective rate of 1.48% on their instant-access deposits.

For those savings in fixed-term accounts, SMEs are earning an effective rate of 3.17%.⁵

Such a high proportion of money being kept in interest-free current accounts suggests SMEs just don't see the rates on offer from savings accounts as being worth the hassle. Or, where better rates are available, SMEs not being made aware of them.

SMEs vs large businesses

It's important to understand what rates banks are offering larger, corporate businesses to gauge their ability to offer better rates to SMEs. Corporate businesses are defined as those with over 250 employees and, as we found out earlier, have a similar amount of cash saved with the banks (£295 billion), despite their smaller number.

Corporate businesses were found to be earning an effective rate of 3.4% on their instant access savings – 1.9 percentage points more than the effective rate made available to SMEs. Fixed-term/ notice account savings, on the other hand, earned an effective rate of 5.7%, which is a premium of 2.55 percentage points when compared to what was offered to SMEs.

Table 5 Savings per SME

	Instant-access	Fixed-term/ notice	Total
SME rate	1.5%	3.2%	2.0%
Corporate rate	3.4%	5.7%	4.1%
Premium offered to corporates	1.9%	2.5%	2.1%

⁴ The chart is based on data from selected financial institutions reported by UK Finance (i.e., Barclays, HSBC, Lloyds Banking Group (including HBOS), Virgin Money (including Clydesdale & Yorkshire Banks), NatWest (including Royal Bank of Scotland), Santander and Co-operative Bank)

⁵ Effective SME interest rates on time deposits has been calculated as the weighted average interest rates across 'Redeemable at Notice' and 'Fixed maturity' deposits. Interest rate on 'Fixed maturity' deposits is calculated as the weighted average of interest rates on deposits with maturity periods <=1 year, 1-2 years and > 2 years

Missing interest

Taking the discrepancy between corporate and SME interest rates into account, Allica Bank estimates that SMEs are missing out on more than £7.5 billion in interest every year. This has been calculated as follows:

- £150 billion of SME savings is currently earning no interest at all sat in business current accounts. This money could be earning rates of up to 3.5% in instant-access accounts made available by challenger banks. This equates to £5.25 billion of lost interest a year.
- £125 billion of SME savings is currently in fixed-term and notice savings accounts earning, on average, 2.1% less than large businesses. If SMEs were offered the same rate as their larger counterparts, they could earn £2.5 billion in additional interest.

It seems that this gulf in the interest rates on offer to SMEs is accentuated by the lack of specialist expertise that these businesses have in-house and the opaque nature of the market itself, making it hard to distinguish between the available options. Large businesses, on the other hand, will often have their own treasury departments, who will have a better handle on the market and be able to shop around for a good deal.

Conclusion

This data highlights the stark difference between the treatment of SMEs and corporate businesses by banks when it comes to their savings, and the huge opportunity to give a £7.5 billion boost to what is such an important segment of the UK's economy and our local communities.

With £150 billion of SME cash earning absolutely nothing in return, there is a clear need to raise awareness of the options available to these businesses. With a further £125 billion earning 2% less than what is being offered to larger businesses, we need to level the playing field by paying greater

attention to what's being offered to SMEs, boosting transparency, and ensuring banks are quickly passing on interest rate rises.

The UK's SME community have had a rough ride of it the past few years, yet have shown time and again over the past decade their resilience in the face of a host of challenges. By closing the gap on corporate savings rates and opening up the market to greater transparency, this research represents an opportunity to provide a well-needed – and well-deserved – boost to their bottom line.

⁶ 3.5% is currently the best instant-access savings rate available to SME businesses. This is provided by Allica Bank as part of its Business Rewards Account.