FXE Technologies

THE GROWTH CHALLENGE

Breaking down the barriers to business finance

SME Lending Monitor Q2 2025

A letter from our Chairman

The UK's economic growth challenge is well trailed and there is no dispute that small and medium-sized businesses will be central to our future economic prosperity.

Having had the privilege to work amongst UK SME for many years I am always blown away by their resilience and entrepreneurial spirit and I've seen so many success stories of adaptability and innovation. I have also seen first-hand how important it is for the UK banking and commercial finance sector to support SMEs growth ambitions with access to appropriate and timely finance. There is no question that over recent years we have witnessed a material increase in the number of funders and an increase in disintermediation as the broker channel has expanded. And the statistics confirm that a more diverse market has translated into greater choice and competition. This has to be good for growth.

However, 'Access to Finance' continues to be an area which is hotly debated. This detailed report from Funding Xchange, who have been providing a funding marketplace to link businesses to alternative funders for nearly a decade, and who have insights into some 500k business loan requests, highlights some of the challenges and opportunities to help more SMEs finance their investment and productivity growth plans. The findings are relevant to all stakeholders who have an interest in driving growth and prosperity in the UK's SME sector, including policy makers, regulators, funders and to SMEs themselves.

Paul Gordon
Chairman of Funding Xchange

The Growth Challenge: Addressing affordability and access in a changing finance landscape

UK businesses have demonstrated remarkable resilience in the face of recent economic shocks – including Brexit, COVID-19, war in Europe, and inflation – reaching a record 5.6 million registered firms by early 2025. However, access to finance remains a significant challenge: access to market-based lending – particularly for working capital – has not recovered to pre-2020 levels.

Initiatives like the Bank Referral Scheme (BRS) have seen limited success: firms lacking a strong credit profile, micro-businesses and startups often face multiple rejections and lack guidance on becoming funding-ready. Without feedback, business owners are left with a sense their 'business is not good enough' – turning many into "permanent non-borrowers."

The core issue is not a lack of supply but borrower readiness and affordability. Many small UK businesses are over-leveraged, especially compared to European peers, and face higher borrowing costs. At the same time, demand has shifted toward short-term survival finance as insolvencies and payment failures rise, reflecting depleted cash buffers.

The lending market has become more competitive and diverse, driven by challenger banks and fintech platforms. However, these gains are threatened by thin margins and regulatory gaps. Lenders to micro-SMEs require scale, automation, and the ability to use personal guarantees – tools that face increasing scrutiny.

To ensure long-term growth and stability, policy must address affordability, borrower readiness, and the need for modern regulation that reflects a rapidly evolving and increasingly digital financial ecosystem.

UK businesses have taken hit after hit. Yet, against the odds, they've remained remarkably resilient.

UK Ltd: A masterclass in resilience or a slow unravelling?

From Brexit to a global pandemic, war in Europe, supply chain meltdowns, and surging inflation – UK businesses have taken hit after hit. Yet, against the odds, they've remained remarkably resilient.

Entrepreneurial spirit hasn't just survived – it's soared. In 2023, the UK hit a record with **880,000 new business registrations, followed by 850,000 more in 2024**, according to Companies House. This means that as of January 2025, the UK boasts 5.6 million registered businesses – a historic high.

This growth is even more impressive considering the environment. The Office for National Statistics (ONS) reports that UK inflation peaked at **11.1% in late 2022 – its highest rate in 41 years**. Meanwhile, Bank of England data shows that the base rate rose from 0.1% in 2021 to 5.25% by 2024. These are conditions that usually choke off lending and business formation.

Despite this, UK lending portfolios appear to be holding firm giving the impression of a robust UK business sector. The Bank of England reports that defaults across SME lending remain broadly stable at **historically low levels** and anticipates that reductions in Bank Rate will relieve some repayment pressure. We have previously commented on the 'replacement' effect that Covid payments have had in lowering default rates as riskier loans were refinanced with government-backed loans but expect that this effect has largely 'washed through' portfolios. The discontinuity of recent years, however, leaves some lenders with **less mature lending portfolios** where overall default rates can be misleading – and cohort analysis provides better insights into performance.

That said, FXE is seeing early-warning signals that have not necessarily translated into rising default rates: lenders are seeing incidents of unexpectedly sudden business failures – companies collapsing without prior signs of distress – as well as a rising number of fraud cases. No consistent picture is yet forming, but some lenders are wondering if these are signs of the toll recent years have extracted from the UK business community.

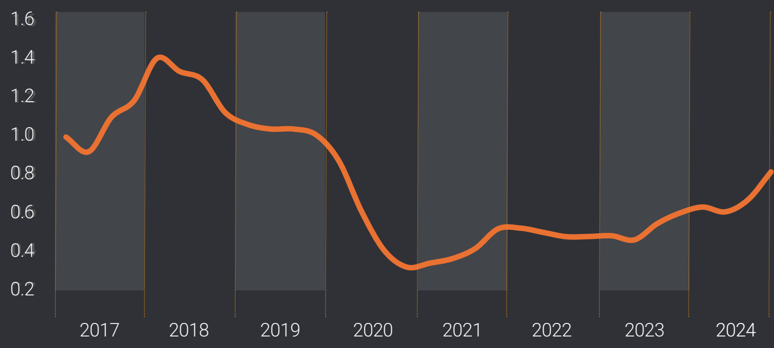
Against this backdrop, market-based lending to small businesses, especially for working capital needs, appears to have recovered slowly.

Source:
1 https://www.bankofengland.co.uk/financial-stability-report/2024/november-2024

Access to market-based finance appears to be recovering for fundable businesses (Gold & Silver Segments)

Our data tracks access to market-based finance (i.e., removing government-backed schemes) for businesses with a fundable profile. The data shows tentative signs of recovery in 2023 and stronger improvements in 2024. But access to finance remains stubbornly below the levels seen prior to 2020. Interventions in the lending market to broaden access to finance have focused on supply-side dynamics – often starting with the hypothesis that banks are not providing the support needed. Yet, as the dominance of banks in commercial lending has been replaced with more diverse lending solutions, access to finance remains challenging.

Success rate of credit applications for fundable profiles (FXE Marketplace)
Rolling 3-period average, indexed to 2017 Q1



Source: FXE Marketplace Applications

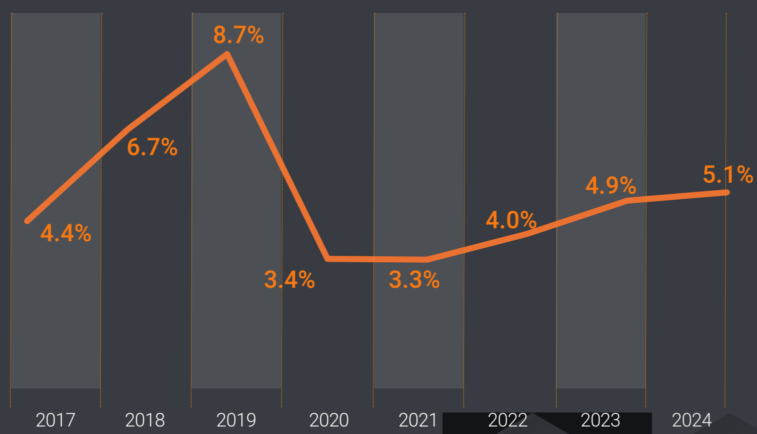
Bank Referral Scheme is only able to support a very small share of businesses that are ready to access finance

The Bank Referral Scheme (BRS) shows that non-bank lenders are unable to unlock significant volumes of finance where banks are not able to help. BRS focuses on providing businesses declined by banks with access to non-bank finance. Yet, broader access has had a limited impact on access to finance. According to British Business Bank (BBB) data, the success rate peaked in 2019 at 8.7% and hovered around 5% in recent years.

Greater diversity may have brought more competition to the funding market – which creates more choice in product solutions and new service solutions – but has not transformed access to finance for small businesses declined by banks – more than 90% are experiencing just another rejection.

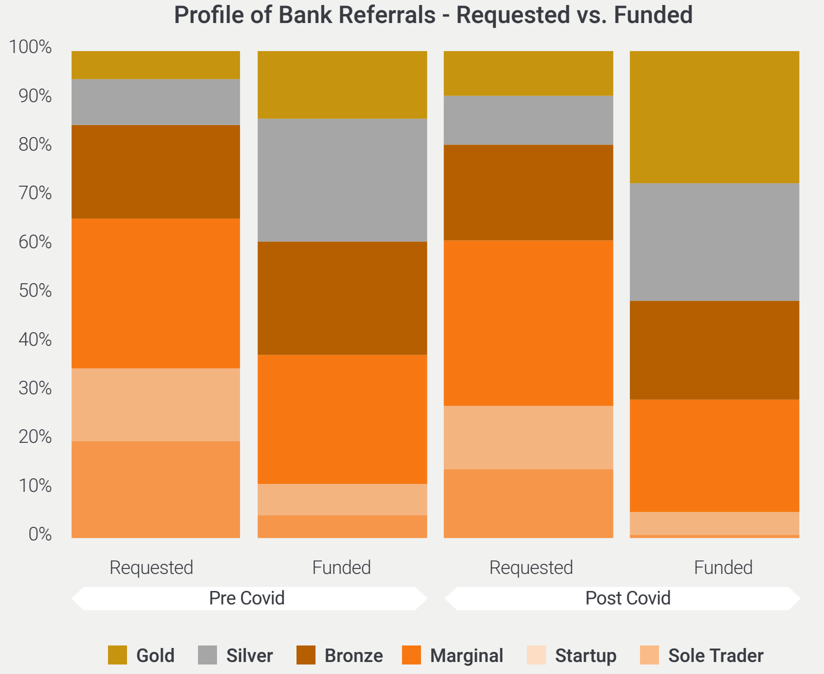
In fact, we can see that today businesses appear to require even stronger profiles to successfully access funding than at any time over the last ten years.

Bank Referral success rate



Source: HMT Bank Referral Scheme: January 2025 publication

Clear shift in the profile of businesses accessing finance through the Bank Referral Scheme[2]



Source: FXE Marketplace Applications

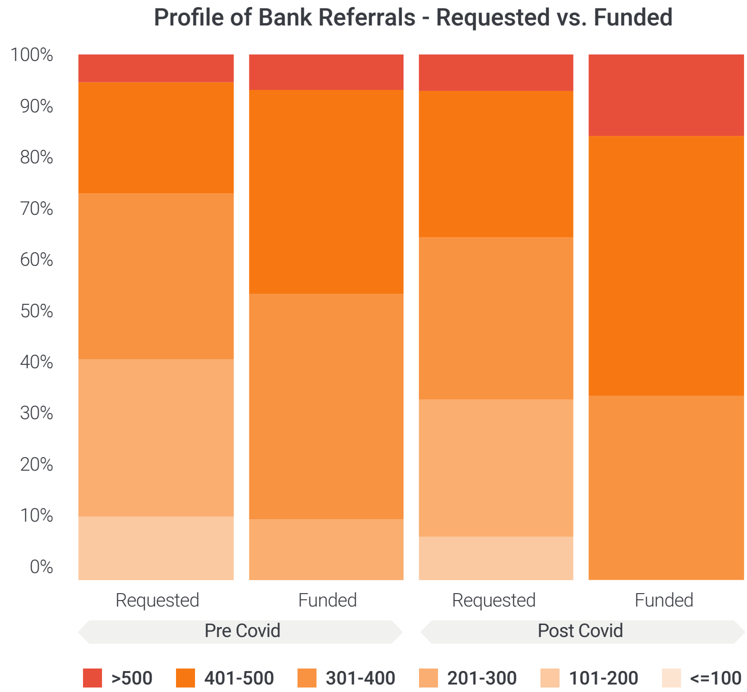
Today more than 50% of businesses funded through BRS have a very strong profile (Gold or Silver) compared to 40% before Covid. The biggest impact of this shift? The success rate of more marginal profiles has halved.

Why are we seeing this shift? The data we are setting out in this report shows that we've moved from a period where more businesses were borrowing to grow – to one where many are borrowing to survive. And with fewer assets to secure loans against, lenders are focusing more on the financial health of the business and the business owner. To access finance, businesses are expected to evidence a track record and business owners need to demonstrate prudent financial management.

This shift can also be seen in the emphasis of personal credit scores ('Director Scores') when applying for business funding.

Personal Credit Scores matter even more post-Covid when accessing Business Finance

Commercial lenders are less willing to tolerate a poor personal score to provide business finance: prior to Covid, 25% of business owners using FXE after a referral had a strong credit score and accounted for 43% of all funded businesses. Post Covid, 33% of referrals had the same credit profile and accounted for 61% of funded businesses. It would be simple to put these changes down to lenders' reduced risk appetite in the face of economic uncertainty: supply side factors like risk appetite, in particular at times of economic upheaval, often determine whether finance is available. Changes in the profile of businesses seeking finance are much harder to pinpoint. This report seeks to paint a more nuanced picture on how the profile of businesses seeking finance is changing – with a shift towards businesses that are not ready to take funding or can't afford additional lending.



Source: FXE Marketplace Applications

Source:

2 Time periods: Pre Covid - Up to 29th Feb 2020, Post Covid - 1st Jan 2023 onwards

A closer look at the demand side of the UK lending market

One element that stands out in terms of the profile of UK small businesses seeking finance since the Covid crisis: they carry significantly more debt than their European counterparts. During the pandemic, the government offered some of the most generous loan support in Europe – about one-third of all UK businesses took out COVID loans, compared to 10-13% in France and Germany. Uptake was especially high among the smallest firms, many of whom accessed up to £50,000 through Bounce Back Loans without any affordability checks.

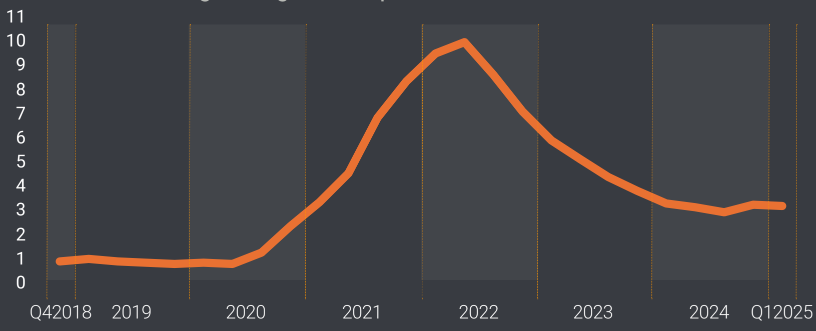
UK businesses seeking access to finance are saddled with high debt levels

Small UK businesses are today servicing debt they didn't carry before the crisis..

FXE Marketplace data provides a window into the businesses that are seeking debt today – and shows that the **median debt-to-turnover ratio spiked during the crisis – and has not returned to pre-crisis level** but appears to have stabilised at more than **twice the level compared to pre-crisis.**

Among businesses that hold debt just over 25% have government-backed loans accounting for at least half of their outstanding debt.

Median indebtedness (Debt-to-turnover ratio)
Moving average over 4 periods, indexed to 2018 Q4



Source: FXE Marketplace Applications

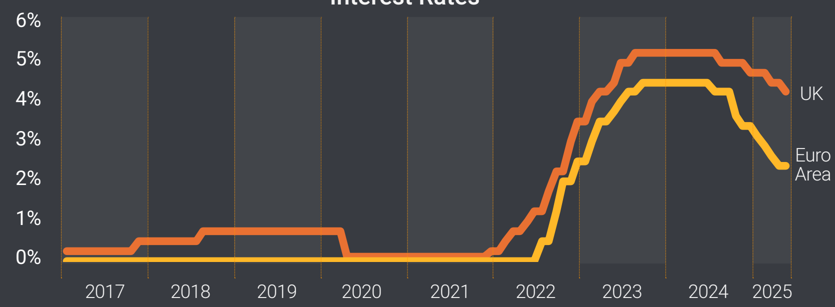
Costs of accessing finance is significantly higher in the UK than in the Euro Area

After years of ultra-low interest rates, the tide turned in 2022 with the surge in inflation. The Bank of England raised rates sharply and hasn't brought them down much since.

As of May 2025, the **UK base rate stands at 4.25%**, while the **Eurozone equivalent is 2.4%**. The difference in base rate appears to be widening - making finance pricier in the UK than in many peer markets.

This means that UK businesses have been hit twice: first, by being saddled with more debt from pandemic-era loans; and second, by higher interest rates, as lenders face increases in costs of funding. As a result, the affordability of borrowing has become a growing challenge.

Interest Rates



Source: Trading Economics

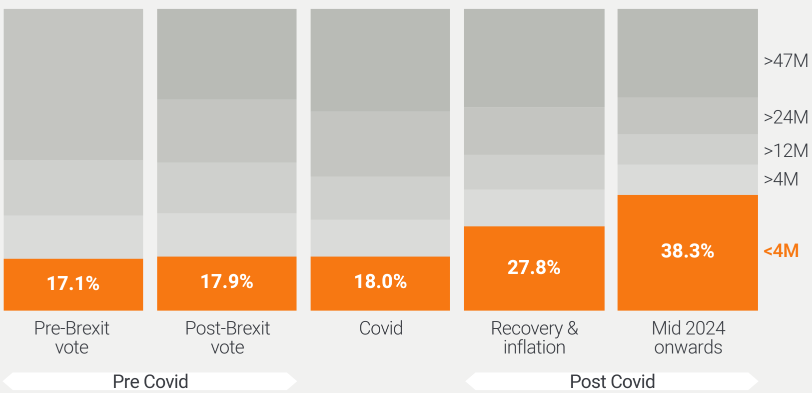
Startups as the Engine of Growth – but aren't loan-ready

Another key shift is in who's applying for funding. A growing share of businesses being rejected are startups – often at a very early-stage.

Before the pandemic, only about **18% of BRS referrals** were companies under four months old. Today, that figure is closer to **40%.** This reflects the boom in new business formation and entrepreneurs' lack of understanding of what makes a business fundable.

Bank Referral Scheme is serving a large pool of businesses not ready to access finance

Share of bank referrals by Trading History



Source: FXE Marketplace BRS Referrals

The problem? Most lenders expect a business to have **at least two years of trading history - and full annual accounts - before offering a loan. Asset-backed lending might come sooner,** but it's not always an option.

There is a government-backed **Startup Loan** programme, but the odds of success are slim: **only around 1% of applicants** introduced by FXE get approved.

So, many startups face a **double rejection** – first by the bank, then by the alternative lenders via the Bank Referral Scheme. And crucially, **they're getting no feedback** on how to improve their chances next time. The result? A growing group of disillusioned entrepreneurs who assume they're "unfundable," when in reality, they may just be too early in their journey.

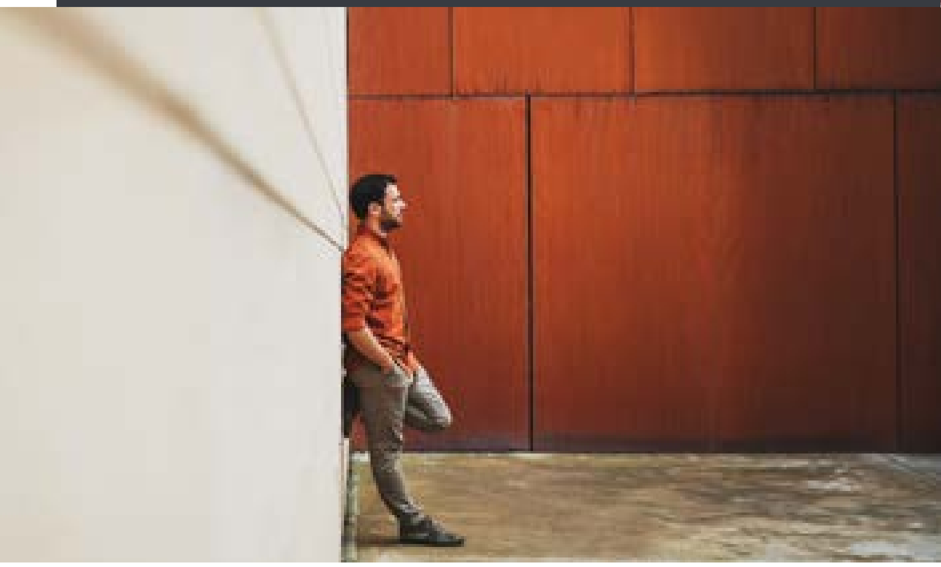
Based on our experience, the impact of the negative experience can be long lasting: businesses believe 'they are not good enough' and will forgo applying for finance in the future.. This mindset, formed in response to a negative experience, is likely to be a significant contributor to many businesses' reticence to using finance to grow – turning them into **permanent non-borrowers.** It is simple to prevent this sentiment from festering – by providing businesses **clear feedback** on what they can do to make themselves more fundable. Sometimes that can be as easy as waiting a few months until the business has filed at least two sets of annual accounts.

A simple 'ageing' analysis of startups introduced by BRS shows that around a third of startups will become eligible for finance once they have filed their second set of accounts. The share of eligible startups easily tops 60% if we also include factors like continued growth in revenues. So instead of declining businesses that are too young, asking them to come back once they have filed their second set of accounts is likely to reduce the stubbornly high share of 'permanent non-borrowers.'

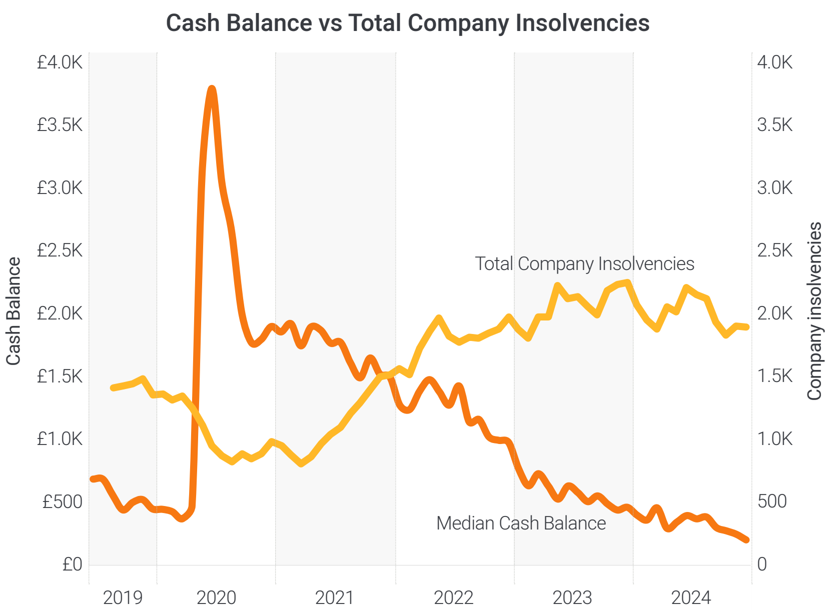
Businesses are getting weaker, not stronger

While the UK Ltd. weathered the pandemic surprisingly well thanks to government support, structural weaknesses have been masked and appear to be re-emerging.

- **Insolvencies have risen significantly,** as the last of the COVID-era cash buffers run dry.
- **Payment failures are rising,** and more businesses are seeking short-term working capital rather than investment finance.



Company insolvencies are creeping up as cash balances held by businesses are falling

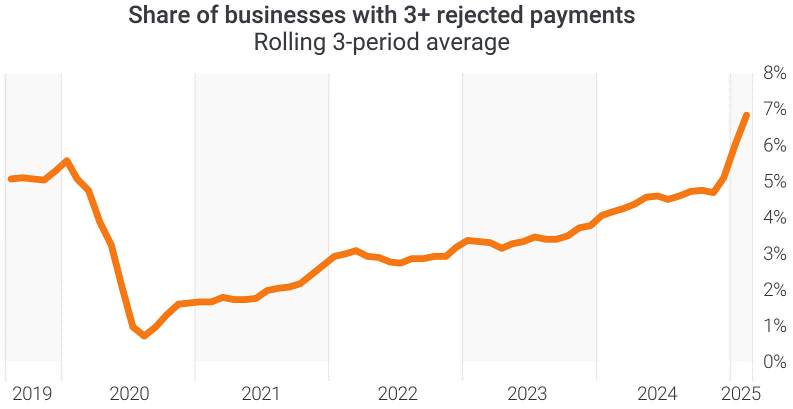


As would be expected, the broad uptake of covid cash allowed a share of businesses to survive for longer. This "cash bump" is clearly visible in the bank accounts of businesses that have used the FXE Marketplace. The bump **temporarily suppressed business failure rates,** providing even struggling firms with a financial cushion.

However, this protective effect has diminished, with **cash reserves declining to pre-COVID levels by late-2023** – a shift that correlates with a noticeable rise in business failures. It is worth noting that median balances are now below the pre-Covid levels – and are continuing to decline.

Sources: Company Insolvencies – "Company Insolvencies, December 2024" published by The Insolvency Service; Cash Balance – FXE Marketplace Applications

Payment distress is rising – now surpassing pre-Covid levels



Source: FXE Marketplace Applications

Unsurprisingly, businesses that are seeing dwindling balances are experiencing a rise in payment distress – as insufficient funds in bank accounts mean that payments are 'bouncing'. This level of rejected payments has now surpassed pre-Covid benchmarks and appears to continue to increase.

As a result, demand for finance has changed dramatically: the availability of covid cash led to a surge in asset finance in 2021, as businesses invested in physical assets like vans, outdoor seating, etc.

As cash reserves dwindle, the emphasis has moved from investment to liquidity-driven lending – essentially, **"survival loans"** aimed at bridging cashflow gaps. Without sufficient assets to secure loans, lenders are placing **greater weight on the overall profile and creditworthiness** of both the business and its owner, rather than relying on the underlying asset value.

What it all adds up to: An affordability crisis

At its core, what we're seeing isn't a failure of lending supply – it's a crisis of affordability and readiness on the demand side.

Historically, affordability has been the reason behind about **40% of business loan declines.** But with today's high interest rates, pandemic debt hangover, and weakening cash positions, that number is likely even higher.

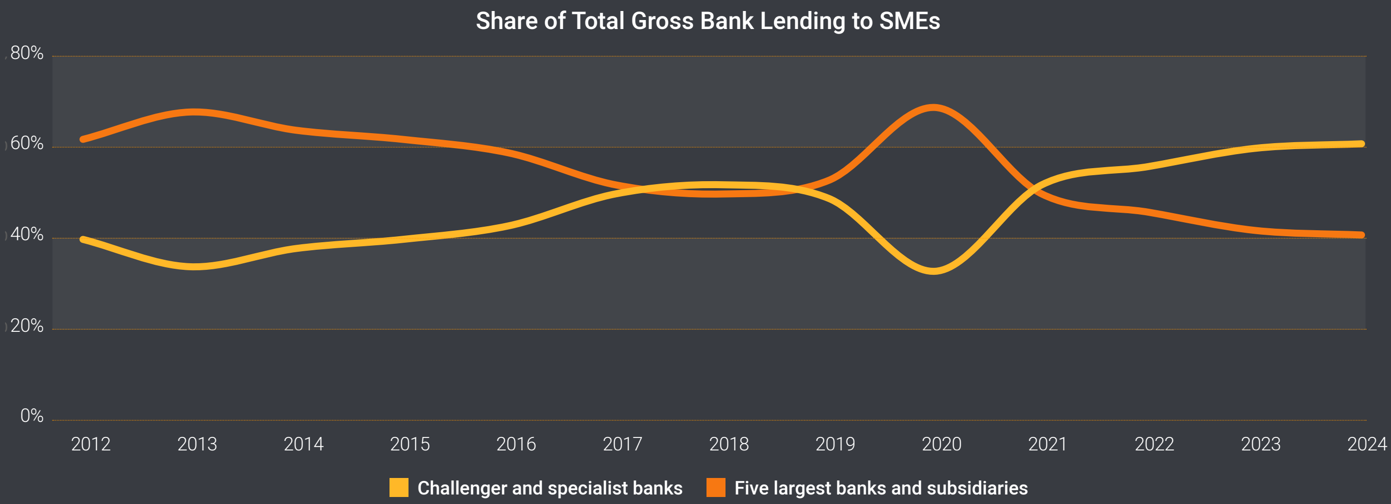
This is especially true for the UK's smallest firms – who make up over **90% of all businesses** and provide **65% of total employment,** yet continue to struggle to secure the finance they need.

The Bank Referral Scheme isn't the problem – but it's also not the fix

The Bank Referral Scheme (BRS) was introduced at a time when large universal banks dominated the UK commercial lending landscape. After years of focusing on capital-light lines like cards and trade finance, these banks were seen as under-serving SMEs. BRS emerged as part of a broader set of government interventions aimed at diversifying the lending sector.

Notably, BRS did not address specific market failures but offered remedies for symptoms – providing businesses a "second chance" to access funding. Other reforms tackled structural barriers to competition, such as unlocking valuable data assets to support challenger banks and facilitating access to debt finance for new entrants. Taken together, these measures have undeniably shifted the market landscape.

Funding landscape is becoming more diverse



Source: British Business Bank "Small Business Finance Markets" Report – p127

Data from the British Business Bank shows High Street banks' share of SME lending has fallen from around 70% in 2013 to just 40% by 2024. However, this headline masks important nuances: UK Finance suggests that banks' share of lending to medium-sized businesses has held steady at roughly 70%. The disruption is concentrated at the smaller end of the market – a segment increasingly served by challengers leveraging automation and deep data analytics.

Dynamic, real-time credit decisioning at the intersection of Consumer/Business lending and payments is unlocking finance in marginal segments that is too costly to provide with traditional lending models. Their growth reflects that the share of businesses on the margins is growing – as more businesses are being founded and fewer businesses in the UK 'graduate' by outgrowing the 'micro' status to become more robust and more profitable. This is not just driven by the 'gig-economy' where employment is replaced by less secure 'gig-jobs' but a long-term trend in the UK as a nation of 'shopkeepers' rather than Mittelstand-Entrepreneurship.

Challenger banks and fintechs have invested heavily in digital technology, enabling faster, more tailored customer experiences while transforming cost-to-serve models. Large banks are acutely aware they must disrupt their own legacy approaches to remain competitive.

There's no shortage of lenders in the UK eager to fund small businesses. Banks, fintechs, and alternative lenders are all jostling to deploy capital, and on the surface, competition seems healthy.

According to BBB's own analysis, 80%+ of COVID-era loan volumes went to High Street banks, crowding out smaller players.

Despite the temporary return to the dominance of High Street banks, the market shifted regardless. Today competition in lending comes from lenders who can move faster, price smarter, and operate with lower costs through a smart use of people facilitated by digital technology. The likes of Allica Bank, Shawbrook, and Funding Circle have stepped in to fill gaps, delivering tailored offers to SMEs and scaling fast – extending the shift of lending from High Street banks to other providers – as well as extending availability of finance into more marginal segments.

In the micro-SME space, funders like Iwoca and YouLend focus on small, short-term financing needs but have seen competition shrink as many lenders exited post-COVID. These models depend on scale and high automation to remain viable, as the economics of small-ticket lending are challenging.

Personal guarantees (PGs) and other security mechanisms play a critical role in extending finance to marginal borrowers. Restricting their use would sharply constrain access, particularly for those already facing the greatest financing barriers. The FCA's Consumer Duty framework offers robust mechanisms to enforce responsible lending and affordability standards; extending these protections to cover all vulnerable micro-businesses and all forms of debt-like finance would strengthen borrower safeguards without unduly limiting access to credit.

What needs to happen?

Despite the increasing diversity in lending solutions and competition, many small businesses continue to hit a brick wall when trying to secure funding. The Bank Referral Scheme brings this dynamic to life: it has contributed to creating a more diverse landscape, but it has been less effective in supporting the over 130,000 declined businesses that have used the scheme – just 4-6% of those introductions result in a successful deal.

The low success rate often gets blamed on the scheme itself. Yet, **most of these businesses simply aren't fundable** – at least not right now. They either can't afford the finance or don't meet basic eligibility criteria.

Even more concerning, the scheme doesn't give rejected firms the information they need to become fundable. Businesses walk away not knowing what went wrong, or what to change. The feedback loop is broken.

If we want to increase successful access to finance, the focus has to shift to:

- **More transparency and feedback** for declined businesses
- **Better support and education** on how to become fundable
- **Smarter policy tools** that recognise the affordability gap and offer realistic stepping-stones for micro and early-stage firms

The real issue isn't lack of lenders. It's that too many businesses are simply not in a position to borrow.

The UK lending ecosystem has transformed – and that's a good thing. A more diverse market means better solutions for businesses. But it also creates new policy challenges.

A safety net designed for a handful of big banks won't cut it in this new landscape. In a future crisis, regulators will need mechanisms to support all systemically important lenders – including specialists who serve high-impact segments.

Looking ahead, we expect increasing collaboration: banks funding specialist lenders – creating broader liquidity pools, as well as collaborating on the delivery of lending solutions to bank customers. Tech partnerships accelerating the digital transformation of banks to enable them to remain relevant in a market that is changing quickly.

This is critical to future-proof a system that has become more diverse and competitive, but where regulation and support mechanisms have not followed suit yet. It is also vital for the sector to support SMEs – not just in a crisis, but as a sustained engine of growth.

FXE Technologies

FXE Technologies offers a suite of digital SME lending solutions that enable banks, brokers and lenders to instantly triage customers against underwriting models while transforming customer conversion and engagement. FXE Technologies' solutions are used by a range of customers including Tier 1 banks and boutique lenders.

View the FXE Technologies solution suite at **fundingxchange.co.uk/fxe-technologies**

Funding Xchange

Funding Xchange has been a leading provider in the digital assessment of SME lending applications since 2014. The Funding Xchange MarketPlace puts businesses in control of their funding, providing access to 70+ lenders from one simple funding request, enabling them to easily compare terms and apply with confidence and not impact their credit score.

Funding Xchange SME Lending Monitor

We believe that collaboration between banks, alternative lenders, digital technology providers and policy makers is vital to ensure businesses have access to the critical lifeline that funding often represents. This collaboration brings together different capabilities, providing business owners with the ease of access to business finance that the consumer finance market has enjoyed for more than a decade.

Through our marketplace, which is used by over 30,000 businesses across the UK every quarter, we have a front row seat to observe any changes in funding needs – and the funding solutions available to them from more than 40 providers.

For further information on our capabilities and to learn how we help small businesses, please visit: **fundingxchange.co.uk**

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