



**UK Factoring & Invoice Discounting
Market Research Summary – Part 2
20th July 2011**

Index

Introduction	2
Raising The Profile of Invoice Finance.....	3
What Is Missing from The Invoice Finance Market?	3
What Customers Don't Like About Invoice Finance	4
What Businesses Expect To Pay For Invoice Finance.....	6
How Clients Suggest We Promote Invoice Finance.....	7
Summary & Conclusions.....	8

Introduction

FundInvoice LLP offer the UK's first market research led invoice finance advice and search service <http://www.fundinvoice.co.uk>. We also publish "FundingVoice" magazine which offers expert tips, advice and articles about improving business cash flow and funding.

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This document summarises that market research findings prior to the 20th July 2011 which while somewhat dated will still be of interest to anyone with an interest in the UK invoice finance industry.

This market research summary is based on a number of individual surveys and is also enhanced with some anecdotal feedback received from businesses seeking invoice finance.

The conclusions of the first research report were:

1. **Invoice Finance Has Growth Potential** – the invoice finance industry has the potential to grow if the profiles of these products and providers were raised with potential customers.
2. **Invoice Financing Costs Are High But Also Misunderstood** – cost is clearly a key issue inhibiting the expansion of the invoice finance market. However to some degree prospective customers may also be over estimating the cost of invoice finance. Promotion of more transparent costing would help.
3. **Product & Brand Awareness Is Low** – greater awareness of the benefits of invoice finance, and of the businesses providing these services, would lead to a greater uptake of invoice finance.
4. **Invoice Finance Can Have Funding Advantages Over Overdraft** – clearly overdraft is currently used far more widely than invoice finance. However, the levels of funding raised through invoice finance, as a percentage of outstanding debtors, can be significantly higher than that available via overdraft. Overdrafts also appear to have been reduced or removed in some cases.

This market research summary follows on from the previous document.

Raising The Profile of Invoice Finance

Our survey of 100 SME's (small and medium sized enterprises) indicated that:

59% of SME's anticipate problems raising business finance during 2011

In 2010 we asked the same question and 71% said the same thing. This suggests an improvement in expectations about the ease of raising business finance, it also remains a strikingly high number of businesses that are anticipating problems finding business finance.

Of those that said they were anticipating problems raising finance we asked them about their reasons. These were their responses:

- 39% Banks are cutting back
- 29% VAT/tax arrears
- 25% Losing customers
- 5% My provider is becoming increasingly cautious & less flexible
- 2% My credit rating is poor

This perception of finance not being available from banks is not consistent with our understanding that some of the major banks are struggling to meet the lending targets agreed with the government.

In addition, all of the reasons given for anticipated problems in raising finance can be overcome via invoice finance which is still freely available, including invoice finance from bank owed providers, even if a business is losing customers, has tax arrears or has a poor credit history. In fact, invoice finance is often the natural solution in these situations where more traditional forms of finance such as overdraft or loans may not be available.

This message is not getting through to the business population which highlights the need for a platform to raise the profile of the invoice finance industry. This will enable a change in the perceptions of businesses from an expectation of problems raising finance to the use of invoice finance as a natural solution.

What Is Missing from The Invoice Finance Market?

Invoice finance industry figures have shown positive signs of growth in terms of the volume of business transacted by clients, although the growth in actual client numbers has been minimal. The various factoring and invoice discounting providers are all competing to grow their relative market shares so this led us to question where the gaps are within the invoice finance market that could be addressed by providers that are looking to accelerate their growth.

We selected a sample of 100 SMEs (Small and Medium Sized Enterprises) and we asked them a simple question - "What is missing from the invoice finance market?".

The answers that they gave were as follows:

- 31% Flexibility
- 28% Instant online setup and approval
- 14% Advertising
- 12% General awareness of what invoice finance is
- 6% Ease of use
- 4% A well known, highly thought of provider
- 2% Personal service
- 1% Money
- 1% Adequate credit limits
- 1% A comparison site

We questioned these businesses further regarding what they meant by "flexibility" and in all cases they were referring to:

The need for additional flexibility in terms of funding, beyond that which presently exists

Clearly, whilst invoice finance already represents a more flexible form of funding than more traditional methods, there is some way to go in order to meet customer requirements when nearly a third of respondents feel this way.

The second highest response was the requirement for "instant online setup and approval". These results appear to corroborate anecdotal evidence that some businesses are now more comfortable with the concept of signing up for financial products online.

Lastly, combining those that responded "advertising" with those that responded "general awareness of what invoice finance is" constitutes 25% of the total number of respondents. This continues to evidence the need for greater promotion of invoice finance as a cash flow solution.

What Customers Don't Like About Invoice Finance

Pure invoice finance funding, by Asset Based Financing Association members, exceeded £12.6 billion at the end of 2010. Therefore, invoice finance is clearly fulfilling the funding needs of a large number of UK businesses.

In order to better tailor our products to meet customer needs, and hence grow the market further, it is helpful to consider business' perceptions of the shortcomings of invoice finance at present.

The research that we have conducted in the past identified that a significant proportion of businesses feel that:

“Cost” is the greatest barrier to increasing the uptake of invoice finance

However, to better understand the other short comings of existing invoice finance offerings, we asked a sample of 100 SME businesses (Small and Medium Sized Enterprises) to put aside cost as an issue and tell us what other aspects of invoice finance arrangements they didn't like.

The results were as follows:

- 20% funding limits
- 18% audits
- 17% unapproved invoices
- 13% paperwork
- 12% personal guarantees
- 7% electronic payments taking 5 days
- 5% upsetting some customers
- 3% time from invoicing to receiving funds
- 3% credit limits
- 2% lack of communication

Funding limits and unapproved invoices, when combined accounted for 37% of the responses. These both relate to additional funding controls over and above the initial payment percentage used to determine the level of funding. These types of restrictions are commonly applied across invoice finance industry and are considered by many to be the cornerstones of controlling risk. However, the fact remains that:

***Funding restrictions were highlighted as “pet hates”
by a significant proportion of businesses***

What is also interesting is that there are several items within this list that can be addressed by products that are already on the market, but perhaps are not well known. For example, “paperwork” was mentioned by 13% of the respondents and there are products which already operate in a paperless fashion. Furthermore, there are providers who are prepared to provide funding without personal guarantees in some situations. Often these niche products may not be obvious to newcomers to the market again raising the issue of product awareness.

In summary, within a market that is clearly already providing significant funding to UK businesses, the above list sets out a number of items that could help some funders make their product offerings even more attractive to prospective customers.

What Businesses Expect To Pay For Invoice Finance

We have also spoken to 100 potential invoice finance prospects in order to understand their expectations about the cost of invoice finance. We asked them what percentage of their turnover they expected to pay for various types of invoice finance such as factoring and invoice discounting.

On average, the businesses:

Expected to pay 3.93% for factoring and 1.97% for invoice discounting

So they expected the cost of factoring to be almost double the cost of invoice discounting. It is clear that in many cases SMEs are also overestimating the cost of invoice finance generally. SME's estimates appear to support their expectations that factoring will be expensive.

We also compared the pricing estimates of businesses that preferred bank owned factors with those that would opt for an independent provider. We found that:

Those that would prefer an independent factor estimated the likely cost of invoice finance to be 57% higher than those that said they would prefer a bank owned provider

This clearly indicates an expectation that invoice finance from an independent factor will be substantially more expensive than that from a bank, which again is not always the case.

These results highlight that potential customer's price expectations are often out of line with reality and we need to continue to work to educate businesses regarding the actual costs of these services.

In another survey, we asked a sample of 100 SME businesses (Small and Medium Sized Enterprises) whether they thought invoice finance generally was overpriced, underpriced or priced about right. The results were as follows:

- ***68% believe that invoice finance is overpriced.***
- 32% believe it is priced about right.
- None of the respondents thought that it was underpriced.

These results reflect the perception that the cost of invoice finance generally is too high. Therefore, we went further and asked the SMEs that thought invoice finance was overpriced to state the amount by which they felt it was overpriced.

Those that thought it was overpriced responded as follows:

- 2% of respondents felt it was overpriced by 5%.
- 10% of respondents felt it was overpriced by 10%.
- 19% of respondents felt it was overpriced by 20%.
- 46% of respondents felt it was overpriced by 25%.
- 2% of respondents felt it was overpriced by 35%.
- 19% of respondents felt it was overpriced by 50%.
- 2% of respondents felt it was overpriced by 100%.

This means that on average:

Customers think that the cost of invoice finance is c.19% too high

Although it is also the case that:

Just over three quarters of the respondents are looking for a price reduction of no more than 25%

...in order to feel that these products are priced “about right”.

This would suggest that there is an opportunity for invoice finance providers that are able to develop low cost methods of delivery in order to enable a reduction of at least 25% on the current average market pricing.

How Clients Suggest We Promote Invoice Finance

Much of our historic research has suggested that one of the key issues for the invoice finance industry is that invoice finance, factoring and invoice discounting are not well known or understood by businesses.

This prompted us to ask a sample of 100 SMEs businesses (Small and Medium Sized Enterprises) the following question: “Our research suggests that invoice finance is not well known amongst businesses, how would you suggest this could be best addressed?”

The answers given to this question were as follows:

- 27% Bank to advertise it as part of banking packages and offers
- 25% Accountants to promote it
- 18% Advertising in business start up magazines
- 9% Telesales
- 6% TV advertising
- 5% Radio advertising
- 3% Mail shots
- 2% Networking

- 2% Companies House recommending invoice finance
- 2% HMRC recommending invoice finance
- 1% The employers pack to feature an article about invoice finance

An initial review of these results suggests that promotion via banks and accountants is most widely considered to be the best way of growing awareness of invoice finance. However, some 43% of the above answers are purely methods of marketing, advocated by the respondents.

Perhaps the most interesting, and possibly overlooked, segment of these results comes from the 5% of respondents that have recommended some kind of government backed promotion e.g. Companies House recommending invoice finance, the employers pack featuring an article or HMRC recommending it.

There is also an interesting thread from the 18% of respondents that recommend advertising in business start up magazines. If at this early stage in a business' development invoice finance were to be promoted and recommended as a main stream solution to funding requirements, these products might be able to assist a greater percentage of businesses.

In summary, whilst at face value these results may seem to suggest a variety of disparate marketing activities, there are some interesting ideas buried within the detail. For example:

A government backed promotion of invoice finance, perhaps to start up businesses or even via the key parties that businesses turn to for advice, such as accountants and banks, could yield significant results

This could have a huge impact on the number of UK businesses that could be helped using these flexible funding solutions.

Summary & Conclusions

To summarise:

- 1) **Customers Want More Flexible, Unrestricted Funding** – with the exception of cost, funding restrictions were the top issues for potential customers. They also wanted more flexibility around the provision of funding.
- 2) **Customers Want Instant Online Setup And Approval** – the second most popular improvement to invoice finance generally was the requirement for facilities to be able to be approved instantly via the internet.
- 3) **Product Awareness Is Low** – customers did not appear to understand the full range of invoice finance products that are currently on the

market. Several of these products that are already available addressed requirements that were raised during the research.

- 4) **Customers Think Invoice Finance Is Overpriced** – by an average of c.19% and a 25% price reduction would satisfy some 75% of potential customers.
- 5) **Banks And Accountants Are Key To Invoice Finance Growth** – potential customers saw promotion of invoice finance via banks and accountants as the key. They also advocated more general industry marketing and felt that government support for invoice finance would also play a role in growing the market.

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