UK Finance

Business Finance Review 2025 Q2

Quarterly commentary on business finance for small and medium-sized enterprises.

September | 2025

2025 Q2 Highlights

UK Finance provides a regular analysis of how the finance needs of small and medium-sized enterprises (SMEs) are being supported through lending from mainstream lenders and specialised finance providers and looks at their deposit holdings. This latest *Business Finance Review* provides a round-up of lending activity to SMEs in the second quarter of 2025.

Executive Summary

- Gross lending continues to see year-on-year growth for the sixth quarter running, but the pace of increase has slowed to eight per cent year-on-year, from 14 per cent in the previous quarter. This slowdown is chiefly weaker lending growth to medium-sized firms – signalled in the contraction in new loan approvals last quarter. Overall net lending continues to inch towards positive territory.

- News on small companies remains positive – new lending in Q2 was 28 per cent up on the same quarter a year ago and this quarter saw further increases in new loan approvals. However, new overdraft approvals have fallen back – likely a consequence of robust growth in the previous six months ahead of April's NICs increase and concerns about broader cost pressures.

- Loan approvals to medium SMEs fell again compared with a year ago – which will likely see further easing in momentum in overall gross lending in the coming quarter.

- Total deposits continue to fall, but at the slowest pace since 2022 Q3. Deposits are now a fifth down on the peak, driven by a rundown in sight deposits. Data continues to show some large sector differences on savings decumulation.

- Overdraft utilisation rates remain fairly static for both small and medium SMEs, while repayments ticked down slightly this quarter – a trend observed across all sectors.

- The overall picture this quarter is therefore one of modest growth and stable delinquency levels in a cautious, cost-conscious business environment, with subdued demand for investment lending. The broader economic outlook continues to present challenges for SMEs from international trade risks, fragile consumer confidence and uncertainty about government policy ahead of the autumn budget.

Economic context

The UK economy continued to expand in Q2 but at a slower pace than in the previous quarter. GDP increased by a slightly better-than-expected 0.3 per cent in the three months to June, following a strong 0.7 per cent rise in the first quarter. Activity at the start of 2025 was boosted by some frontloading of activity ahead of the US tariff announcement in April, with the significant boost from net trade, in particular, fading in Q2.

Output growth slowed across both manufacturing and services. Starting with production activity, manufacturing output was buoyed at the start of the year by increased production across almost all sub-sectors, in part a response to customers seeking to secure goods ahead of the possible introduction of US tariffs at the start of Q2. In the end, tariffs on most countries were postponed until Q3 while negotiations on framework trade deals with the UK and other key markets continued. The effect was a slowdown in activity in Q2, with sentiment in the manufacturing sector, including more recent PMI surveys for the start of the third quarter, remaining in negative territory.

Across service industries overall quarter-on-quarter growth slowed from 0.7 per cent in Q2 to 0.4 per cent in Q1. The easing in growth rates was fairly board-based across service industries – but notably wholesale and retail, and professional and scientific services. This was offset, somewhat, by a solid quarter of growth in hospitality and rising activity in health and social care. Increased public spending on health and defence should continue to provide a prop to growth in the second half of this year.

In contrast, growth in construction output strengthened in Q2, supported by both new work – mostly infrastructure, and repair and maintenance – primarily private housing. Despite growth reported in official statistics, the construction PMI points to ongoing challenges across the sector, such as lower volumes of new business and weaker customer confidence, which are weighing on the growth outlook for the coming year.

Indeed, surveys from across the economy are signalling a number of potential headwinds for businesses including US trade policy, uncertainty about the UK fiscal outlook and sluggish domestic demand. The news on US tariff policy changes frequently, from a framework deal with the UK on the one hand, to new product-wide charges on steel, and court challenges to President Trump's policy on the other. The Decision Maker Panel survey reports that around half of business cite tariff uncertainty as one of many sources of business uncertainty, with near one in ten saying it is one of the top two or three risks.

There are wider uncertainties about the outlook for the US economy, risks that tariffs could fuel higher inflation remain, but the labour market is slowing, and concerns are

mounting about the erosion of Federal Reserve independence, which have contributed to recent turbulence in bond markets.

Concerns about the UK tax burden also have not faded as the NICs increase came into force in April. The ONS BICS survey reports that around one in eight businesses (with more than nine employees) are concerned about taxation. With another budget around the corner and ongoing worries about the state of the UK public finances, business will be looking for the Chancellor to meet her fiscal rules without any additional tax increases on the private sector. UK borrowing costs and Sterling are also at risk of an adverse market reaction should the budget leave question marks about the sustainability of government borrowing.

In response to these risks and challenges business investment fell back in Q2 and recruitment activity has softened. Unemployment has been edging higher this year and the number of vacancies in the economy has been in steady decline, with reports of leavers not being replaced and mounting concern about forthcoming employment law changes, according to a KPMG/REC survey.

The loosening labour market and associated easing in pay pressures, was however, a factor for some MPC members voting to cut Bank Rate at the August meeting. The decision to cut borrowing costs by another quarter point was a close call against the backdrop of high and rising consumer price inflation.

While the committee has been split on rate decisions over the past year, August's decision was unusually close with four members voting for a 25-basis point cut and one preferring a larger 50-basis point cut. The argument for a cut was that progress on domestic disinflation continued and there was more evidence of a cooling labour market and subdued demand outlook. As such, less restrictive monetary policy was warranted. The remaining four MPC members, however, remained concerned about elevated inflation and risk of second round effects on wages, and voted to hold Bank Rate at 4.25 per cent.

Markets are now judging another cut this year to be less likely, but the Committee minutes stress that policy is not on a pre-set path and will be driven by how the incoming data evolves. The Bank of England's latest forecast expects inflation to tick higher in the coming quarter, but its GDP outlook was broadly unchanged with growth of 1.25 per cent in 2025.

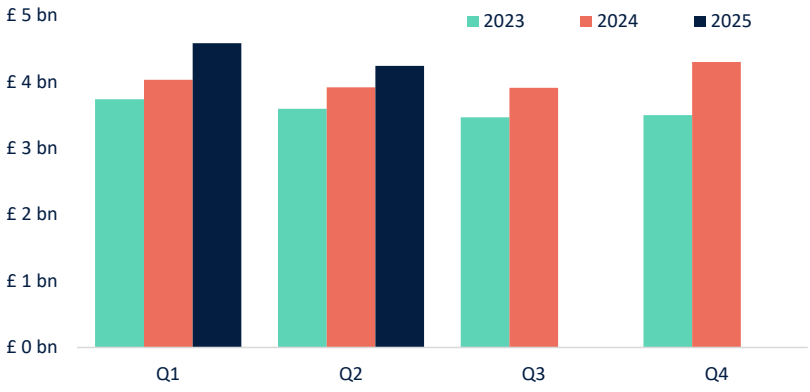
Lending to SMEs

2025 Q2 marks the sixth consecutive quarter of year-on-year growth in gross lending by the main High Street lenders, continuing the gradual increase in new lending to SMEs since the lows seen in the second half of 2023. In the three months to June lending by the main banks totalled £4.24 billion. This growth aligns with the steady rise

in new loan approvals we've also reported over the past year and a half. However, the pace of increase in lending growth, at just over eight per cent compared with a year ago, eased further this quarter, down from 14 per cent last quarter and the slowest since the start of 2024 (**chart 1**).

The easing in the pace of growth is, perhaps, not surprising given the economic context outlined earlier. In the first half of this year businesses have faced into higher employment taxes, cautious consumer demand and significant volatility in global trade policy. Against this backdrop, business surveys have pointed to waning optimism and fewer companies report plans to grow (see, for example, the SME Finance Monitor), which will be contributing to cautious investment plans and a potential pause or delay in borrowing activity.

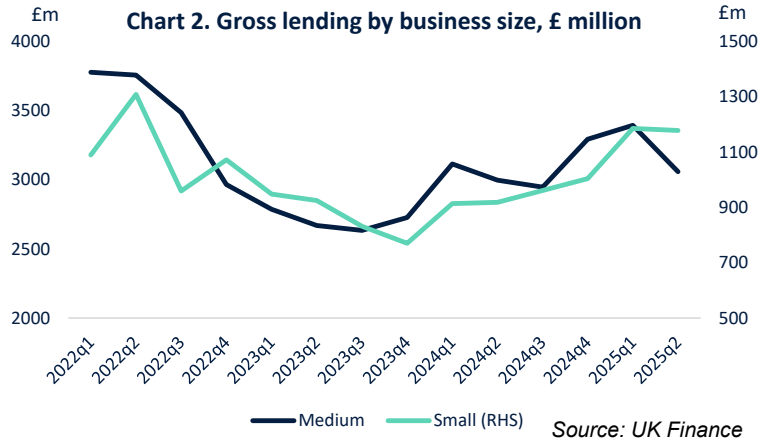
Chart 1. Gross lending to SMEs, £billion



Source: UK Finance

Notably this quarter our data points to some divergence in lending trends between small- and medium-sized SMEs (**chart 2**). New lending to medium-sized firms dipped in the second quarter compared with the previous three months, though it was still two per cent higher than the same quarter in 2024. In contrast, gross lending to the smallest companies (with a turnover up to £2million) was 28 per cent higher than the same quarter a year ago, a similar pace of increase to that seen in the previous six months.

Chart 2. Gross lending by business size, £ million



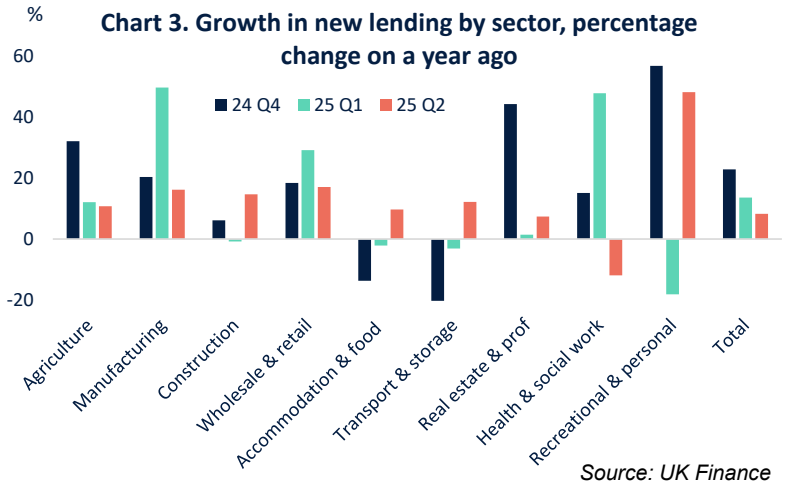
Source: UK Finance

This divergence was signalled in our finance approval data last quarter. We noted in the first three months of 2025 that the number of loans approved to medium firms was down on 2024 Q1, whereas there was still some momentum in approvals to smaller businesses, and as we'll turn to in the next section, this trend was sustained in the second quarter of 2025.

With gross lending ticking higher than last year, net lending is also inching back towards positive territory. Overall net lending stood at -£1.1billion, up from -£1.2billion

in Q1 and, excluding the pandemic, the highest since the end of 2019. The increase was driven by the smallest businesses, with net lending to medium SMEs hovering close to balance in the first half of 2025.

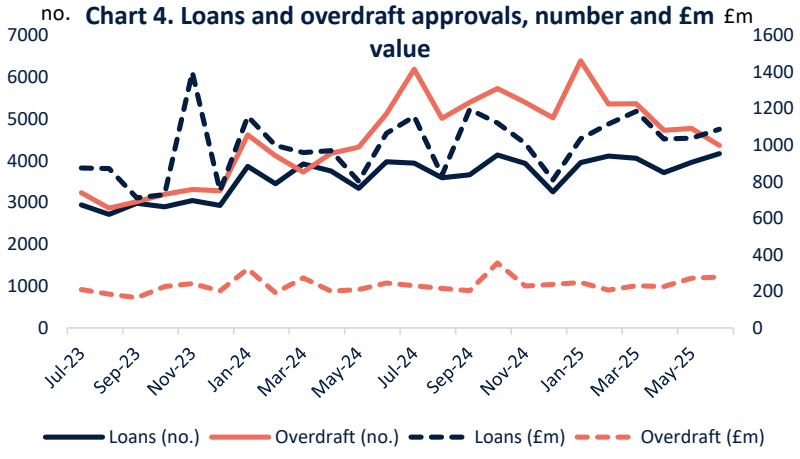
There was little to separate lending growth across different sectors this quarter (**chart 3**), with rises broad based across almost all sectors, with the exception of health and social work, though this contraction followed solid growth in the preceding three quarters. Accommodation and food, and transport and storage sectors, had seen falls in lending in the previous two quarters, but this reversed in the most recent quarter. Elsewhere, rises have been largely steady in the first half of 2025; more muted growth as most sectors are dealing with similar worries about the near-term outlook.



Source: UK Finance

New finance approvals

Continued increases in the volume and value of finance approvals in the most recent quarter (**chart 4**) suggests some further momentum in new lending in the coming quarter. The number of loans approved in the quarter was seven per cent up on a year ago, equating to an 11 per cent increase in the value approved – similar to the growth rate in the previous quarter. However, it is becoming more apparent that demand for, and approval of, new overdraft facilities is coming off the boil. The number of overdrafts approved was the lowest for a year, though there was a rise in the value of new overdrafts approved. Easing in the requirement for new or increased overdrafts may reflect a surge in demand in the previous quarter, which was likely a precautionary



Source: UK Finance

measure for some SMEs worried about the cashflow impact of the incoming NICs increase and other potential cost rises coming from trade disruptions.

Indeed, as **chart 5** illustrates, overdraft approvals to both small and medium-sized businesses were roughly the same or lower in 2025 Q2 compared with a year ago, though the slowdown was much more significant in approvals to the smallest firms, with the value of facilities approved the lowest since the beginning of 2024.

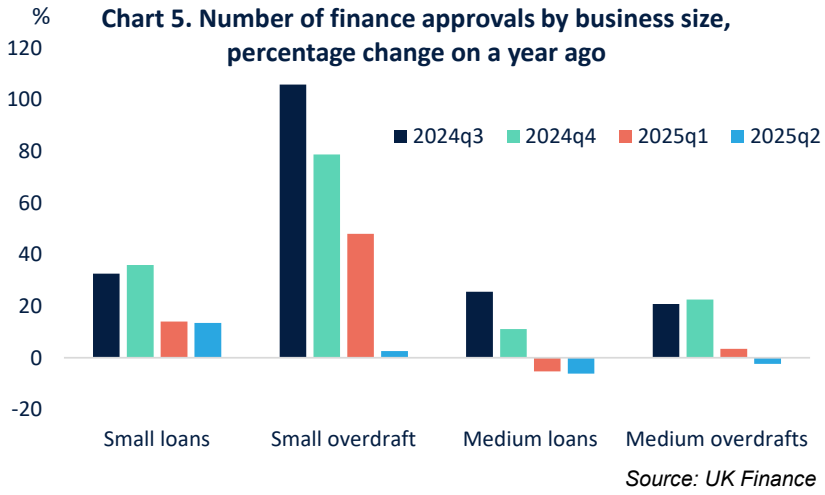


Chart 5. Number of finance approvals by business size, percentage change on a year ago

Source: UK Finance

The trend in loan approvals by business size mirrors that seen in the previous quarter. The number of loans approved to small firms was 14 per cent up on the same quarter a year ago, providing further evidence that High Street lenders are providing finance support to the smallest firms, with the value of these loans up some 15 per cent, though this does represent something of a slowdown on the previous year. However, loans approved to medium sized companies fell, year-on-year, for the second quarter running.

Turning to new finance approvals by sector (**chart 6**) year-on-year increases in the number of loan and overdraft facilities approved was again fairly consistent across industries. The few exceptions included agriculture, which saw a particularly notable drop in overdraft approvals in the year to Q2.

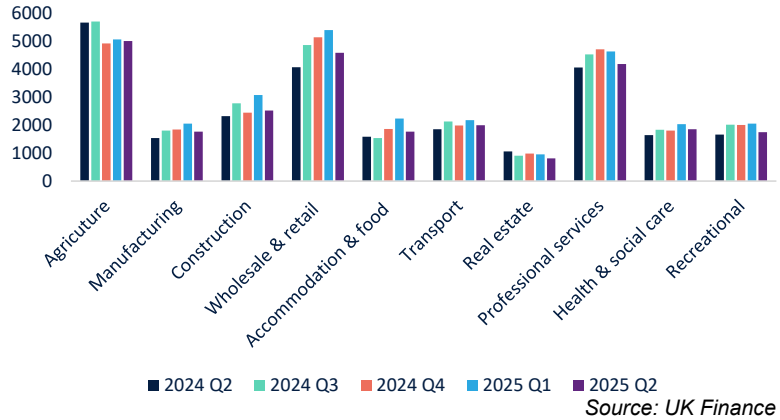


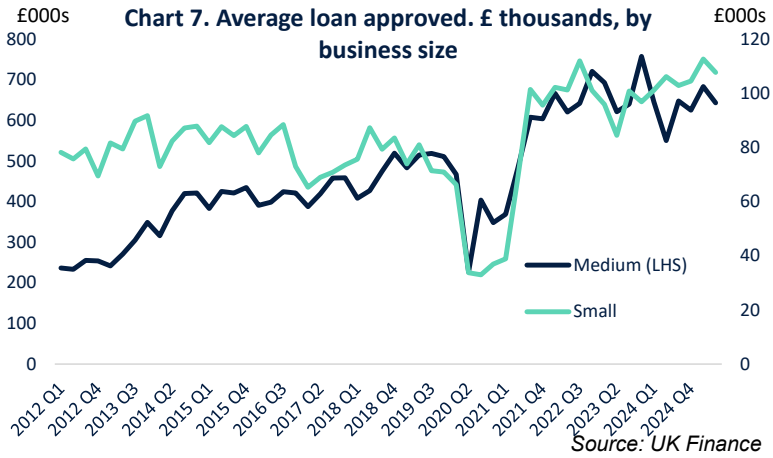
Chart 6. Finance approvals by sector, number

Source: UK Finance

Accommodation and food also recorded a larger than usual seasonal slowdown in overdraft approvals, but this was offset with a solid expansion in new loan approvals for hospitality SMEs. There was, however, a drop in approvals to real estate SMEs of around a quarter compared with a year ago – this was seen in both new loans and overdrafts. Stamp duty tax

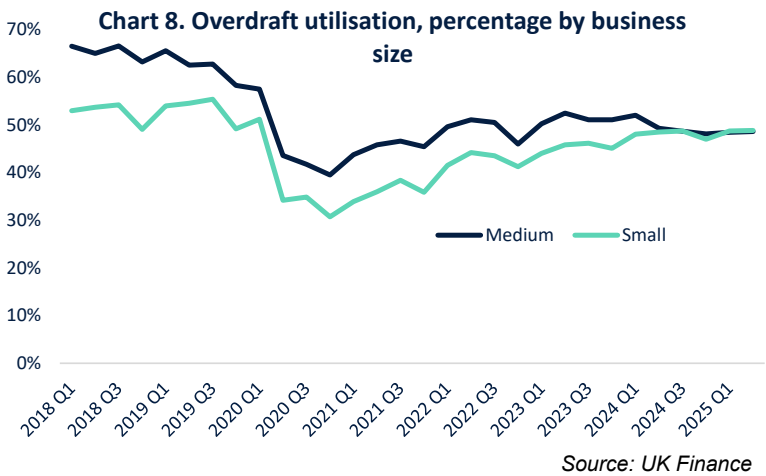
changes, which took effect in Q2, likely had the impact of pulling some activity forward with demand for finance waning as the changes took effect.

Finally, **chart 7** looks at the average value, in current prices, of loan finance approved to small- and medium-sized enterprises. Following the post-Covid rebound in the average facility approved to smaller businesses, new approvals have been averaging around the £100k mark. In real terms, this is not materially different from that approved between 2016-2018 (equivalent to around £90k in constant prices). However, the average approved to medium-sized businesses has increased in recent years, both in current prices and real terms. This could be a combination of demand and supply factors, with expansion or investment in new technology requiring greater levels of finance as well as lender appetite for larger SMEs.



Source: UK Finance

Utilisation of existing facilities and deposits



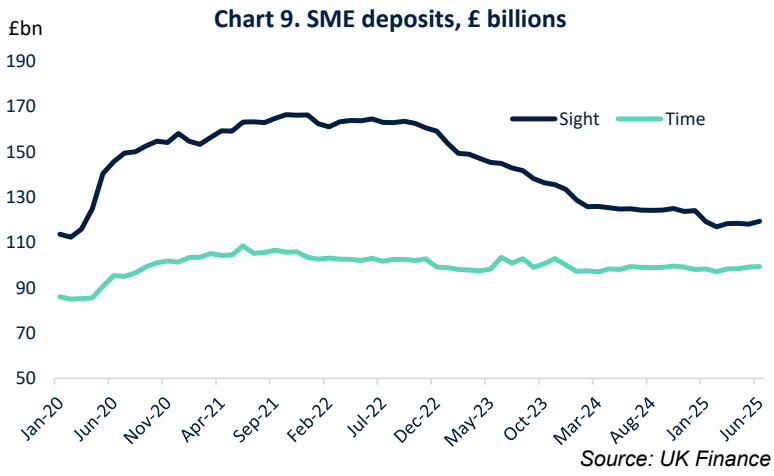
Source: UK Finance

Since the end of the pandemic the trend on facility utilisation has been incredibly stable. On overdrafts, this has not changed in the most recent period (**chart 8**). Despite some strong growth in approvals for new or increased facilities, utilisation rates continue to flatline at just under 50 per cent. This has been consistent for small and medium businesses for more than a year. While we do see some seasonal movements in utilisation data, in the most recent quarter there were no notable movements by sector.

In aggregate, therefore, facilities are there if needed, but even with the growth in new approvals in recent quarters the number of accounts in an arranged overdraft with the main high street lenders remains below that recorded at the end of 2019. And for those with a facility, thus far there hasn't been much sign that SMEs have needed to make greater use of them beyond managing day-to-day cashflow.

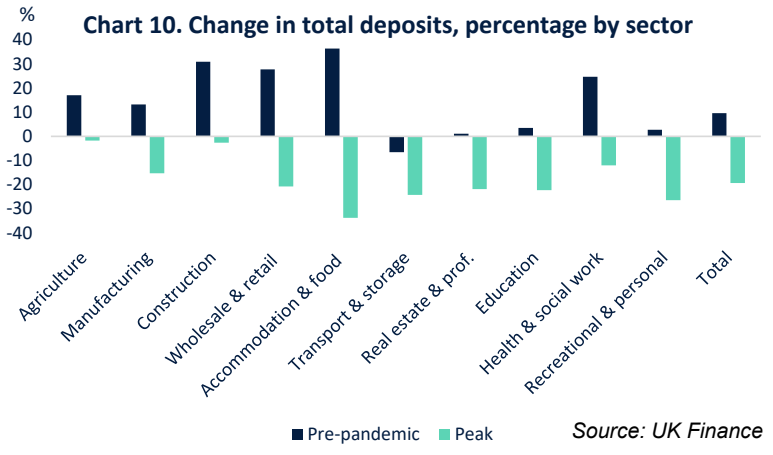
It's still early days for the NICs increase and surveys have indicated that more than half of businesses would seek to pass the rise on through higher prices. Many SMEs will have the headroom within existing arrangements to navigate this and other pressures, if needed.

Turning to SME deposit holdings, we do, however, continue to see greater sectoral variation. Firstly **chart 9** shows a further slowdown in the rundown of deposits, with the total some 2.4 per cent lower at the end of 2025 Q2 compared with a year ago. This was the slowest pace of decline since 2022 Q3 and down from a 2.8 per cent fall in the previous quarter. Overall, deposits have fallen by a fifth compared with the pandemic peak in 2021 Q3, driven almost entirely by sight deposits but total deposits nevertheless stand around ten per cent higher than the start of 2020.



Source: UK Finance

Chart 10 looks at how deposits have evolved across different industry sectors. There has been relatively little movement over the past four years across agriculture and construction. Whereas transport and storage, real estate, recreation and personal, and education now all have deposits close to pre-pandemic levels. Hospitality, however, has seen the biggest decline from the 2021 peak. Inevitably, within these broad sectors there will be significant variation at the individual firm level, and the SME Finance Monitor, for example, reveals that SMEs in hospitality, transport and other services have been more likely to describe themselves as struggling than average. The erosion



Source: UK Finance

of the deposit buffer over the past couple of years is likely contributing to some of these industries coming under more pressure when managing costs and thinking about future plans.

Repayments

Repayments fell slightly in the last quarter (**chart 11**), to £5.4 billion from a quarterly average of around £5.75 billion over the previous year. Declining repayments over the quarter were consistent across both small and medium-sized businesses. The only sector outlier is transport and storage, which saw a more material decline in repayments.

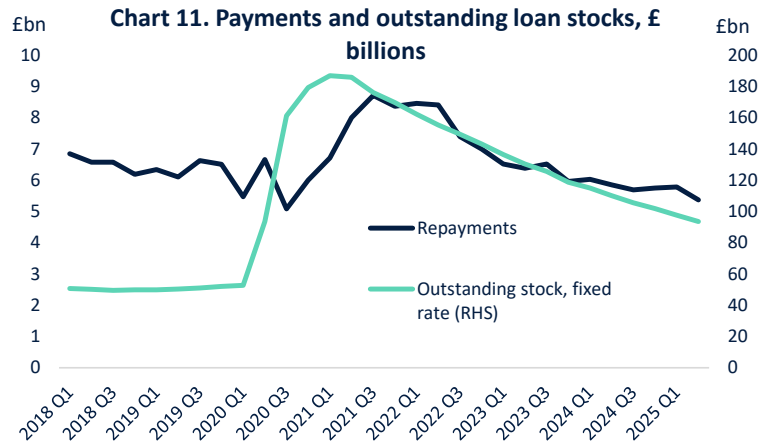


Chart 11. Payments and outstanding loan stocks, £ billions

Source: UK Finance

SMEs that accessed government-backed pandemic funding will be continuing to pay this down. Government data shows a gradual increase in the proportion of facilities that have been fully paid – at the end of 2025 Q1 (the latest available) 15.4 per cent of facilities had been fully repaid and 53.5 per cent are on schedule for repayment. This is continuing to drive down the outstanding stock of borrowing on fixed rates. The stock of outstanding lending on variable rates, which will likely include much of the new lending by the main High Street lenders in recent quarters has been broadly stable over the past year.

SME finance outlook

The first half of this year can be characterised as modest growth in SME lending and stable delinquency levels as businesses remain cautious in a cost-conscious business environment with still weak demand for investment lending. Looking ahead these factors seem unlikely to change materially.

The international environment is expected to remain challenging and closer to home consumer sentiment is improving but remains tentative. The ONS BICS survey indicated that businesses are no more likely to be expecting growth in the year ahead than they were at the start of the year and slightly more businesses are expecting turnover to be the same or lower than was the case a year ago.

Against this backdrop, we might expect to see a further slowdown in lending growth in the coming quarters. In addition, we may see greater sectoral variation in lending trends as export-focused industries deal with tariff realities and labour-intensive ones continue to manage higher employment costs.

In addition, businesses will also be looking to the forthcoming autumn budget in which the Chancellor is again expected to have to take action on spending or tax to ensure fiscal rules are met. Any further measures that add to the cost of doing business will offset any positive action to support SMEs set out in the government' recent Small Business Strategy and would weigh further on new investment.