

EXTRACT

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## SME BANKING

# Banks and SMEs – a developing partnership

By David Cavell

A new report by RBR, *SME Banking: Best Practice and Case Studies*, identifies the critical success factors for banks seeking to develop a profitable share of the SME market.

## An economically important role

The definition of what constitutes a small- or medium-sized enterprise (SME) varies across the world. The formal definition adopted by the European Union recognises three types of SME, namely:

- Micro enterprises with less than 10 employees;
- Small enterprises with 10 to 49 employees; and,
- Medium-sized enterprises with between 50 and 250 employees.

In the EU, micro businesses account for 92% of SMEs and employ an average of two staff. They also provide employment for 30% of the total private labour force. Across the globe, the numbers may vary by country, but there is universal recognition of the importance of the sector to both national and local economies.

The global market is now recovering from a major economic downturn, and many banks are now taking the view that the worst is over. They are renewing their long-term interest in the SME sector, and upgrading their strategies accordingly. Dexia Bank in Belgium exemplifies the many institutions actively re-energising their strategy.

However, research shows that there are many lessons to be drawn from the experiences of the last few years, and remedial action is required to repair fractured relationships. The defensive strategies adopted by many banks in the economic downturn have damaged their relationships with SME clients. In the USA, research by Greenwich shows the extent to which banks' brands have been compromised by the perception that the banks lessened their interest in and support for

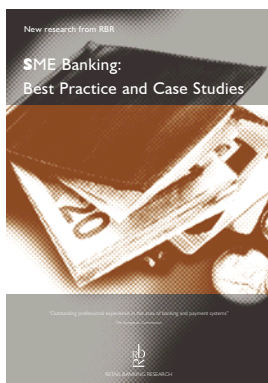
SME customers at a time when it was needed most. Nearly 90% of SMEs felt that banks were facing a serious crisis of trust with their customers.

## Relationship management – getting closer!

The common factor across banks that have continued to enjoy a good reputation has been a strategy of getting closer to their clients. The UK's award winning LloydsTSB, and the equally lauded KeyBank in the USA, which takes a major interest in the Women in Business segment, both talk of the value of a close client-banker relationship.

Indeed, KeyBank takes the view that working closely with its customers has better enabled it to understand their clients' businesses and assist with the particular difficulties of the last few years. Increasing focus on the SME sector has inevitably led to a greater understanding of the role of women as business owners. Within the US market, both the banks and sector advocates have worked to develop and promote an understanding of the impact and needs of the segment. KeyBank's strategy of being a major player in supporting the development of women in business is now entering its third decade, and its commitment was formalised in 2005 through the launch of the award winning Key4Women programme.

A number of banks have also followed a relationship-based strategy through investment in relationship managers and branch staff. TD Canada Trust has invested considerable resources in the development of their branch staff and are now also deploying well-trained small business advisers in their local outlets. In Australia, ANZ Bank is increasing the number of small business advisory staff across their branch network. Dealing with SME clients at the branch is also part of the strategy of the Sparkassen, German community banks. The Sparkassen dominate the provision of financial services for SMEs in Germany. Elsewhere, the Erste Group, a major player in



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eastern Europe, is amongst a number of banks that manage their SME business clients from independent commercial centres.

The development of direct channels also opens up the potential to take a segmented approach to relationship management. Research across Europe by UK based Finalta shows how certain SME segments at the lower end of the scale are now being managed through direct channels with less face-to-face contact. Customers access relationship managers by phone and e-mail. Middle market clients are often served from a pool of relationship managers, whilst the highest value SMEs are often the only ones that continue to have a dedicated officer to support them.

### **Access to finance**

There are undoubtedly justifiable concerns in many countries about the reduced availability of finance for SMEs. Research conducted in Britain by the Forum of Private Business and Graydons showed that up to 40% of applications for finance made by respondents had been declined. A further worrying trend was the high proportion of innovative businesses that were unsuccessful when applying for finance to support the development of their ideas.

In many other markets, banks are managing to sustain a significant supply of lending to the sector with approval rates typically running at around 80%, still in line with historic norms. ANZ, LloydsTSB and Keybank are amongst those that have been willing to make large tranches of finance available, often investing significant resources to ensure that creditworthy clients take full advantage of the available funds. Each bank has targeted its increased lending to the sector in billions, often with fresh commitments as a previous tranche is exhausted. Caja Navarra in Spain has taken financing to a new level. The bank promotes a European competition to encourage innovation in new technologies. Significant capital support including equity finance is made available to winners and other qualifying participants.

Behind these lending strategies, Experian, a major international supplier of credit management and decision systems, believes that the varied nature of the SME sector still poses challenges. Risk assessment techniques similar to those used in the consumer sector have less relevance.

### **Products and education**

The industry is well served by an extensive portfolio of banking products, supplemented by those from specialist subsidiaries (e.g. leasing, insurance). Government lending schemes, where more marginal cases are still within guidelines, are readily available in many markets.

However, research has identified widespread weaknesses within the banks' adoption of the payment card products that could be made available for business clients. The offerings developed by MasterCard Europe during their longstanding commitment to the small business sector have included new card product packages, a formal programme of research, and consultancy. But as yet, many of these worthwhile opportunities remain to be realised.

Some principal players in the sector do offer a wide range of education and business aids to their clients. Most SMEs can turn to the banks for assistance with almost every facet of the running and development of their business. The internet has added an extra dimension through the growing number of webinars and electronically delivered communications such as newsletters and briefings. These are beneficial for both the bank and its SME customers. For example, Bendigo Bank in Australia has experienced a virtuous circle where the promotion of better run businesses has carried benefits for the communities in which the SMEs operate.

### **Delivery channel strategy**

The branch continues to be the principal delivery channel for the SME sector. In the UK, LloydsTSB has experimented with branch-based business lounges, whilst in Spain Caja Navarra have allowed their SME clients to use many of their local facilities, such as meeting rooms. IXE Bank in Mexico and HSBC have created branches dedicated solely for use by business clients. Self-service facilities available for business clients have continued to improve, with automated note acceptance at ATMs. Fast acceptance of notes and coins within an integrated standalone depository is well established, particularly in Europe, as are cash exchange devices.

The advent of online home and office banking, and the growing capabilities of mobiles have brought many benefits. Call centres make up the direct banking delivery mix. However, whilst ongoing

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- ▶ relationship management might be handled through e-mail or other means, there comes a time when face-to-face contact is preferable for either or both parties. This then takes the customers back to the branch or the relationship manager's office.

#### **Small business is good business!**

Many banks have developed well-rounded strategies for building their share of the SME sector, often including a quantified commitment to lending. Moreover, figures from a number of sources suggest that the level of accepted applications is still holding up at around 80% in many markets. Notwithstanding this progress, many SMEs have developed opinions of their banks that are at their lowest ebb, and there is ground to be made up. Variations amongst businesses are too great to

allow the development of a generalised view of the drivers of account profitability across the sector. However, margins on lending can be firm, there is good potential for commission-earning sales and cross-sales, and the new channels are gradually moving clients into a more cost-effective do-it-yourself approach to everyday transactions. These are the ingredients for a profitable banking business, and are only thwarted when, for whatever reason, the bank sustains credit losses. The availability of good margins and the return of economic progress will ensure that, once again, small business is good business. ■

*David Cavell advises banks and building societies around the world on the development of profitable delivery channel strategies. Contact: djc\_laffans@btinternet.com*

**Many SMEs have developed opinions of their banks that are at the lowest ebb**

## **IRANIAN PAYMENTS**

# Electronic banking in Iran reaches turning point

**From one of the region's smallest electronic banking markets at the beginning of the decade, Iran has now become the largest**

#### **Iranian electronic banking market evolves in splendid isolation**

Iran occupies a prominent position within the Middle Eastern electronic banking market if only because of its phenomenal growth rate (particularly over the past five years) and its great size. From one of the region's smallest such markets at the beginning of the decade, it has become its largest, now comprising 19,200 ATMs, 1.3 million EFTPOS terminals and 106 million payment cards (although almost all of these are debit products). This gives it the highest number of ATMs, EFTPOS terminals and debit cards of any country in the Middle East. Moreover, its debit cardholding ratio – at 1.7 per adult – exceeds that of most European countries; and while Iran's density of ATMs and EFTPOS terminals – at 320 and 22,000 respectively per million adults – may not be particularly astounding, they both exceed the world average.

Western card marques are not permitted in Iran, so no truly global international cards such as Visa or MasterCard are issued or used in the country. The Iranians have thus created their own electronic payments infrastructure from scratch called Shetab. The domestic banks now have transaction management systems which resemble those in other countries but which were developed from in-house/internal bank networks. Despite this isolation, cards linked to the Shetab network can also be used at ATMs and EFTPOS terminals in certain other Middle Eastern and Asian countries via GCCNET (the electronic payments network linking terminals across the Gulf region), including Bahrain, China, Kuwait, Qatar, Saudi Arabia and the UAE. Similarly, cardholders from these countries can also use their cards at Shetab terminals in Iran.

Shetab was established in 2002, and now all card issuing banks are required to connect to the system. At the time of its inception, however,

