

Description for the general public

In the proposed research project we investigate relationships between banks and small and medium-sized entities (SMEs). We take into account two aspects of those relationships: **their determinants as well as economic consequences**. Firstly, we intend to identify factors which push given groups of companies into relationships with specific bank types (e.g., local, cooperative banks, on the one hand, or supra-local, commercial banks, on the other hand) as well as factors which determine the specificity of those relationships (e.g., their length, scope and exclusiveness). Secondly, we will check whether a strong relationship with a bank is beneficial for a company.

It is commonly believed that a bank with a relational business model has a competitive advantage in collecting, processing, and communicating soft information about its clients. In other words, a strong relationship with its client allows a bank to better understand the client's financial needs and to assess its loan application even in case of limited availability of hard financial data. Nevertheless, the existing empirical evidence suggests that stronger relationships can have also negative consequences. Firstly, relational **banks may irrationally keep alive financially distressed companies**, i.e., a strong relationship with a bank may lead to a situation in which the distressed company is less financially constrained (i.e., the soft budget constraint hypothesis). Secondly, **a strong and exclusive relationship with a bank makes a company the bank's "hostage"**, and consequently, the bank may be inclined to exploit the relationship in order to impose adverse terms of cooperation on the firm (the hold-up problem). In our research we intend to analyze the abovementioned phenomena with the use of data describing: (a) tens of thousands of Polish SMEs, (b) individual banks cooperating with those companies, (c) local markets in which the companies are located, and above all (d) data identifying both entities involved in each relationship (a bank and a company) and describing specificity of their cooperation.

Our project is likely to significantly influence the current state of the art concerning bank-firm relationships. We find at least two reasons for such a claim. Firstly, the literature about determinants and consequences of a bank-firm relationship in emerging countries or in Central and Eastern Europe is very modest. Secondly, findings concerning other markets are inconclusive. Thus, our research project will help to unravel those ambiguities.