CURRENT TRENDS IN THE APPROACH OF THE CREDIT RELATIONSHIPS BETWEEN BANKS AND COMPANIES

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Abstract: *The relationship between bank (as lender) - company (as debtor) observed as an ensemble of processes and information flows, has always been a favourite subject of study and analysis of both economics and specialty practice, emphasizing a constant concern for improvement considering its importance for the quality of economic and social life of a nation. The management of the lending activity at the banks level has many common features at the company level. In both types of organizations is required the implementation of a decision-making system to guide about the following aspects: the maximum amount of credit that may be granted, the type of credit and the maximum amount which should be granted considering the credit risk.*
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1. INTRODUCTION

Considering the importance of the companies and banks for the national economy by generating of the real flows and respectively by intermediating of the financial flows, all the positive and negative implications arising from lending relationships that are formed between these two institutional categories affect the quality of economic and social life at the macro level.

In the specialized literature, there are several ways to approach the subject of bank-company relationship lending, depending on the items on which the research was concentrated:

- Management of the corporate lending activity (analyzed as system) and the credit control as its primary function;
- Credit as a process, the credit risk management and the techniques and methods for its monitoring and mitigation;
- The accessibility of bank lending to companies with a focus on the history (length) of the relationship between the bank and the enterprise;
- The analysis of the company's creditworthiness and solvency based on its available financial information (hard information) or non-financial information (soft information), difficulties occurred in collecting of this information in case of small and medium enterprises;
- Comparative analysis of the lending activity between of small and medium enterprises and large corporations;

- The importance of bank - company lending relations in social and economic development of a nation.

2. MANAGEMENT OF THE CORPORATE LENDING ACTIVITY AND THE CREDIT CONTROL

The major objectives of the management of the corporate lending activity consist in protection of the investment, on the one hand and cash flow optimization, on the other hand. An important function of management is represented by the credit control. Graham Alastair (former chairman of the British Committee on Standards in Public Life, during the period of 2003 – April 2007) and Brian Coyle (former director of BPP Training, the largest professional training in Europe) have approached this aspect from the perspective of the decisional process necessary in credit sizing and for assuring the observing of the negotiated terms and conditions.

The credit control is essential for avoiding the lack of liquidities as a result of excessive investments and to achieve an optimal balance between the profitability and the afferent risks. Structurally, the management of the corporate lending is seen as a system consisting in the following elements:

- management of the payments / receivables cycle;
- establishment of some secured payment methods;
- credit insurance;
- organizational - planning and risk management systems;
- credit policy;
- credit analysis;
- credit limits and terms.

3. CREDIT AS A PROCESS

The companies' lending activity as process was one of the main topics analyzed by Professor Joetta Colquitt (professor at Mercy College and FT Knowledge and professional trainer, with more than 20 years expertise in the analysis of international transactions, corporate and financial and credit risk). He sought to highlight the specific features (in terms of credit risk management) of each of the two major types of lending approach as a process: classical or traditional and modern.

Thus, according to the classical approach of the credit process, the concept of credit risk management aims to ensure the necessary capital for lending activity and reserve forecasting properly with assessment of borrowers

From the perspective of the modern approach of the lending process, the credit risk management is considered to be a dynamic application in which all aspects of the credit risk are built around of a process of measurement and evaluation of the loan portfolio, process which is in a permanent deployment.

4. THE IMPORTANCE OF THE HISTORY OF RELATIONSHIP BETWEEN THE BANK AND THE ENTERPRISE

The statistical analyzes performed by Ginés Hernández-Cánovas (associate professor at the Polytechnic University of Cartagena - Spain, Department of Financial Economics and Accounting) and Pedro Martínez-Solano (professor of finance at the University of Murcia - Spain, Faculty of Economics and Business, Department of Management and Finance) on lending relationships between banks and companies in Spain, in terms of their age, have revealed two fundamental aspects:

- companies which have a rich history of the lending relationship with a certain bank benefit by an easier access to financing from that bank but with higher costs;
- companies operating through several banks obtain cheaper loans, thus establishing a limit of the concentration degree on a particular bank.

However, the results of these analyzes demonstrate the fact that the presence of a trust between the bank and the borrowed company contributes to the improvement of the access to finance and to the diminishing of the related costs. This is because it increases the probability of providing by the company of the guarantees required to secure the bank loan. Consequently, it is demonstrated that the relationships based on trust represents a better strategy for improving of the companies' access to the bank lending than a richer history or a higher degree of concentration on a particular bank.

In Germany, the strong lending relationships between banks and small and medium enterprises play a key role in the financial and banking system. Erik Lehman (professor at the University of Augsburg - Germany, Faculty of Business and Economics) and Doris Neuberger (professor at the University of Rostok - Germany, Department of Economics and the German Institute for Economic Studies Berlin, director of economic research at Institute of Financial Services of Hamburg and leader of the research group at the Centre for the Study of Demographic Change of Rostok) focused their researches on the social relationships that are established between the loan officers and the companies' managers. In this sense, the two authors have postulated that a lending relationship depends both on the transactions itself and the interactions between the negotiating partners.

An empirical analysis of the bank lending for small and medium enterprises in Germany showed that the loan price is influenced not only by the enterprises characteristics and the credit risk variables, but also by the social interactions between the loan officer and the company's managerial team. They vary significantly according to the age of the company and to the position of the bank compared to the other financing banks of the company (whether or not the institution is the main bank, *house bank*).

In this respect, the companies included within the age class 2-6 years receive significantly lower credit costs because the risk of insolvency is higher. The variables such as mutual trust and obligation have a more important role in the relationships between the company and its main bank than the case of the normal lending relationships with other banks. Thus, the first focuses more on borrowing costs than on cross-selling to be rewarded for the services provided, while the seconds are based on cross-selling as a compensation for guarantees (smaller) received from companies. As is the case of the predecessors, the two authors cannot support the theoretical assumption that the cost of credit depends on the length of the credit relationship.

One of the basic characteristics of the relationships between banks and companies in Italy, is the distribution of a company's exposure on several banks (multiple-bank lending). Giuseppe Vulpes (senior economist in the leadership of Planning Unit, Research and Risk Management and advisor to the CEO of UniCredit Banca d'Impresa Italia) was interested to analyze the determinants of this practice. In this regard, the research conducted by him revealed the significant role of the governance' particularities at the company level.

In particular, it appears that firms which adopt a less formal governance model - which could indicate a lower informational transparency and generally a lower level of protection of third party creditors - are characterized by a higher degree of distribution of their exposure on multiple banks.

Thus, we could say that this practice is the result of an attitude of risk aversion of banks and it represents an assurance mechanism for banks to overcome the difficulties occurred in corporate clients assessing. This observation is particularly relevant for medium-sized companies which, on the one hand, presents corporate governance characteristics similar to the small companies and, on the other hand, shows a distribution of degree of bank exposure similar to the large enterprises.

This may have important policy implications. Indeed, much of the scientific literature on the bank - company relationship highlights that the exposure distribution on multiple banks, the intensity of it, is associated with a lower availability of credit especially in adverse cyclical conditions (known as the rationalization of the loan). This is especially important in light of the capital requirements imposed by Basel agreements.

5. HARD INFORMATION AND SOFT INFORMATION

An improvement in the banking sector's ability to measure and manage risks may reduce the necessity to share the exposure as s solution for limiting of the uncertainty regarding the real level of the risk of the borrowers. An equally important role to achieve these goals is carried by the progress that companies need to do both in terms of information transparency and corporate governance. The conclusion is that those companies that are not able to improve their model of governance risk as in the near future to face a significant tightening of credit conditions.

The small and medium enterprises in the U.S. and many European countries are limited in terms of the ways in which they can financing its activity. Unlike the large companies which can turn to capital markets, the small and medium enterprises have to rely heavily on the bank loans to cover its financing needs. This is because the small and medium enterprises, unlike their larger counterparts, are not audited accounting and must not publish its quarterly or annual financial statements.

In other words they do not provide quantitative information (hard information). In these circumstances, in order to be able to fundament its lending decisions, the banks must use a different type of information, known in banking as qualitative information (soft information) and aiming the skills and the experience of the management team, the quality of the ownership, the company strategy, the market share, etc.

The difficulty of collecting by the financial intermediaries of such information as well as the high costs involved represented the starting points of the research conducted by Timo Baas (assistant professor of macroeconomics at the University Duisburg-Essen - Germany, Department of Economics) and Mechthild Schrooten (professor at the German Institute for Economic Studies, Berlin). They have developed a theoretical model to analyze the behaviour of banks about the credit costs, model that revealed the fact that the lack of reliable information leads to sensible higher lending rates, even if between the company (as borrower) and the bank (as creditor) there are long-term relationships. The analysis thus provides a theoretical explanation for why the managers of the small and medium enterprises consider the external financing as a major impediment to their business development.

The theoretical and empirical work suggests that loan officers have a role in relationship lending by producing qualitative information about their customers. Furthermore, it is assumed that loan officers produce qualitative information that cannot be easily transmitted and that this leads to a greater credit availability for borrowers. However Hirofumi Uchida (professor of banking and financial institutions at the University of Kobe - Japan, Department of Economics), Gregory F. Udell (head of the Department of Finance and Banking - Kelly School of Business at Indiana University, USA) and Nobuyoshi Yamori (professor at the University of Nagoya - Japan, School of Economics) showed that, in case of Japan, this assumption is not valid. The possible explanations could be found, on the one hand, in the fact that the social environment of Japan favours a credit culture in which the transmission the qualitative information from a loan officer at the other is much easier and, on the other hand, in the possibility that the lending relationships are not so important on the Japanese loans market for small and medium enterprises.

6. THE ROLE OF LENDING RELATIONSHIP BANK - COMPANY IN SOCIAL AND ECONOMIC DEVELOPMENT OF A NATION

Despite of various alternatives to cover the capital needs arising from current or investment activity, for most of the companies, the bank loans represent the main source of funding. This dominance is assured by the advantages offered by the bank funding for the company's economic and financial situation:

- obtaining additional funds to support their current projects or the long-term development;
- establishing a relationship with a renowned financial institution facilitates the access to other products and services provided by that bank or other commercial banks;
- increasing the visibility of the company and the degree of confidence in the viability of its business to other potential investors;

- there is a high flexibility regarding the amounts involved, the manner of use of those amounts, prices and terms of repayment of principal and payment of interest;
- the need to convince the bank business viability or simply filling in the credit file may cause the company's management to analyze the business objective to obtain a clear picture of its financial situation and an array of weaknesses, strengths, opportunities and threats which characterize the firm etc.

Considering the role of the banks and companies in assuring of a favourable socio-economic development of a nation, a new philosophy of the bank - company relation focuses on the implementation of team spirit between the relationship manager (bank employee) and financial manager the company, so that they can create value in the mutual interest of the parties and in this way to positively influence the macro-economy.

This becomes more obvious in cases the economy has periods of overheating or recession. In such moment it is necessary that the lending relationship between banks and companies to keep a balance between the expectations of both parties, the people involved having a role in this respect by promoting actions to maintain or restore the trust as a fundamental aspect of the credit relationship.

Thus, during the depression, adoption by banks of a more relaxed attitude in access to finance for companies would have the effect of reducing or at least of limiting the widespread mistrust that block the normal flow of the real economy. On the other hand, in terms of expansion of the economy and financial markets euphoria, the promoting of the lending procedures based on principles of caution would avoid the economy's engines overheating and diminish the amplitude of the future down slope of economic cycle.

7. CONCLUSIONS

The lending relationship between the bank and the company is more than a simple contractual agreement, its correct image being a set of information and operational flows based on trust and transparency, on well grounded decision processes, on accountability and assumed risks. During their performance the lending relationships between banks and enterprises may face with balanced periods but also with periods of stress. The way in which the moments of crisis are overcome directly influences the quality of the relationship, respectively its positive or negative effects on these two types of institutions and furthermore on the real economy

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