

# Executive Summary

## The Influence of the Regional Bank System on Financing the German Mittelstand

Jonas Löher and Christian Schröder

IfM-Materialien Nr. 267

Institut für  
Mittelstandsforschung

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## **Executive Summary**

The study examines whether the regional banking system in Germany has an impact on small and medium-sized enterprises' access to bank financing. We selected the banking system in the United Kingdom (UK) for comparison, because lending is done there in a different way. Thus, in UK a few large banks organize lending centrally from London, while in Germany savings banks and cooperative banks organize lending for small and medium-sized enterprises (SMEs) regionally.

### **Access to finance depends on SME specifics and access to information**

On the one hand, access to credit is influenced by company characteristics including age, size, innovation activity, growth, sector and the macroeconomic environment. On the other hand, existing information about the company also play a major role: the risk of limited access to bank loans is particularly high for young, small and innovative companies due to the asymmetric information between the entrepreneur and the potential lender. With increasing level of relevant information lenders will find it easier to make a risk assessment.

### **Advantages of spatial proximity of regional banks in Germany**

The high density of branches in Germany means that regional banks are in close proximity to their small and medium-sized customers. This proximity facilitates the personal contact between the regional credit institution and the resident SMEs. Client advisors of a regional bank receive much more soft information such as personal views about e.g. the managerial skills of the entrepreneur. Compared to their UK counterparts they have much more possibilities to bring soft information into the credit decision: Due to the proximity between information generation (carried out by the client advisor) and decision-making (carried out by the back office/supervisor) these information can be considered through communication between the adviser and back office.

### **Entrepreneurial personality as a deciding factor**

In practice, it turns out that the credit adviser of a regional bank, in contrast to its British counterpart, has significantly more opportunities to incorporate his subjective assessment into the credit decision. Thus, critical individual cases between credit advisers and sales support are discussed. Exceptional situations including crisis situations, capital-intensive expansion plans or restructur-

ings and their causes can therefore be taken into account in the lending decision.

### **British SMEs do not benefit from the efficient lending process**

The advantage of the central banking system in the UK is its high efficiency in processing credit inquiries. The lending processes have a comparably high degree of standardization. However, this efficiency gain, for example, does not pay off in the form of lower interest rates for SMEs: the interest rate level for business lending in the UK is not lower than in Germany.

### **The regional banking system proves itself in the crisis**

Before the financial and economic crisis, SMEs in Germany and the UK had similar good access to bank credit. Since then, however, significant differences occurred. Thus, bank loans in the UK were much harder to obtain for different types of companies after the crisis. In addition, German regional banks expanded their loan volumes during the crisis. By ensuring credit supply, the regional banks contributed to the high competitiveness of German companies after the crisis.