Bank commitment to an entrepreneur facing the risk of bankruptcy

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Abstract: An extensive body of work explains the basis of bank decisions at the time of entry into a relationship. In contrast, there has been far less research on the evolution of bank relationships over time. In the present study, we attempt to understand how a bank responds when a small business client begins to struggle and faces the risk of bankruptcy. To this end, we conducted a qualitative study on the single case of a French mutualist bank. First, our model on bank commitment highlights the oscillation and arbitrage over time between a business management and a risk management rationale. It then underscores the importance of intuition for small business advisors. This intuition or ‘feeling’ depends on the meaning that small business advisors afford to the entrepreneur's financial difficulties, and the entrepreneur’s attitude as a manager and client. In addition, we enrich the relational lending model by raising the issue of the psychological contract between the small business advisor and the entrepreneur for example.

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Introduction

A bank's decision to finance a company proceeds from a combination of actors and lending technologies (Berger and Udell 2006). In such a process, the mobilization of both hard and soft information strengthens the quality of the decisions made (Berger and Udell 2002; Grunert et al. 2005).[1] However, banks are inclined to base their decisions on financial ratios or scoring systems (Petersen 2004) as information obtained through the client relationship is deemed unverifiable and manipulable (Godbillon-Camus and Godlevski 2005).

This hard information approach is unsuitable for small organizations, which lack the capacity to provide short-term and updated financial data (Bruns 2004). The bank's ability to collect soft information thus becomes a source of competitive advantage, especially in the SME market (Berger and Udell 2002), where the latter is perceived by banks as a central activity (de la Torre et al. 2010). This observation highlights the need for a better understanding of how these subjective elements affect the way banks make their decisions (Grunert et al. 2005). Yet, despite the considerable literature on banks' decision-making processes, the inner workings of bank commitment have still not really been clarified. In view of the lack of knowledge on the way loan officers collect and analyze information in the course of a relationship, additional research is still required (Lehman and Neuberg 2001; Lipshitz and Shulimovitz 2007).

Ignorance of what happens during the relationship is even more marked in the specific case of client companies falling into difficulty. Yet such situations are frequent in the world of entrepreneurship, since failure is common among small business ventures (Ucbasaran et al. 2013). Before bankruptcy becomes inevitable, entrepreneurs have to deal with all the intrinsic

[1] Three dimensions make it possible to distinguish hard information (e.g.: balance sheets) from soft information (e.g.: good impression): the nature (quantitative vs. qualitative), the collection (impersonal and context-independent vs. personal and context-dependent) and the cognitive factors (notions such as judgment, opinion or perception are absent from hard information vs. they are an integral part of soft information) (Godbillon-Camus and Godlevski 2005). Hard information is therefore deemed objective and soft information subjective.

challenges to avoid failing (Phillipart 2017). In this study, we thus use the term "entrepreneur in difficulty" to describe the case of an entrepreneur facing the risk of bankruptcy.

Among the explanatory factors for bankruptcies, an entrepreneur's ability to manage the financial dimension occupies a central place (Thornhill and Amit 2003). In this context, relationship lending is more appropriate (Berger and Udell 2002), both for the bank, which collects more information and is better able to manage the situation (Bruns 2004), and for the company, which receives more support and improves its management of financial aspects (Beck et al. 2018). The quality of support thus determines access to loans for entrepreneurs in difficulty (Freel et al. 2010). It is therefore surprising that such a central issue in corporate life has received so little attention in studies on bank commitment.

Our research question thus consists of opening the black box of bank decisions in a bid to gain further insights into how banks support small businesses in difficulty. More specifically, we try to understand how a bank decides to terminate, maintain or reinforce its commitment to struggling entrepreneurs. Indeed, the literature provides few details on bank reactions in this kind of situation, where the relational and subjective dimension is particularly important, to the extent that behavioral biases appear. This point deserves greater attention because, like entrepreneurs, banks face the risk of escalation of commitment.

Methodologically, escalation of commitment has frequently been investigated through experimental studies. Such approaches tend to decontextualize the decision (Sleesman et al. 2012), and we follow the recommendations of these authors by conducting a qualitative case study of BPro, a French mutual bank. Our main contribution consists of an integrative and dynamic model of bank support for struggling entrepreneurs. It thus contributes to a better understanding of the way the relationship functions and its impact on decision-making. It goes beyond the limits of a deterministic model in which the decision is taken as an isolated, decontextualized and disembodied event. Our work thus provides insights into how soft information is built up as a product of the ongoing relationship between a loan officer and an entrepreneur.

After reviewing the existing literature on bank commitment and bank support for small businesses in difficulties, and justifying the theoretical interest of our research question (1), we present the characteristics of our qualitative methodology in detail (2). The results of the analysis of our interviews and the documents collected (3) are then discussed in order to highlight the main contributions of this study (4).

Literature Review

Lending as a Bank Commitment

According to Berger and Udell (2006), lending as a bank commitment involves technological and organizational measures to assess and control the default risk of the client firm. In practice, rules and discretion represent two extremes of a continuum of lending technologies, which can be classified according to the relative weight of the objective and subjective elements of client support (Cerqueiro et al. 2011), ultimately giving rise to two ideal-typical models (Berger and Udell 2002).

The transactional model values hard information, in other words, relatively objective criteria such as financial ratios, scoring and guarantees (Petersen 2004). In this model, the bank assigns little power to the loan officer, considering that delegating authority to the latter exposes the bank to an increased risk of default (Behr et al. 2011). This gives rise to greater lending standardization and an impersonal relationship between the business and the bank-as-an-organization (Liberti and Mian 2009). The financial institution’s capacity to accompany its clients as closely as possible – through refined and specific knowledge of the small business's capacities – is thus reduced (Berger et al. 2005).

In contrast to this approach, support in the relational model is based on relations between the loan officer and the client company. Relationship lending places greater value on soft information (Berger and Udell 2002). This subjective information often remains the property of the loan officer since it is not easily observable, verifiable or transmissible to others (Stein 2002). Moreover, it is costly to collect, and requires the development of subjective intelligence (Stein 2002). The quality of decisions stems from the fact that loan officers are delegated to collect and evaluate information about their clients (Bruns et al. 2008). Due to the opacity and informational asymmetry, loan officers use their personal judgment on many aspects of the decisions made, particularly in the case of small businesses (Bruns et al. 2008).

Moreover, loan officers' decisions are guided by intuition (Lipshitz and Shulimovitz 2007), i.e. a "*vague feeling of knowing something without knowing how or why*" (Hayashi 2001:60). The applicant's professional background, the nature of the market, the strategic project, the reasons for the loan application, the logic and sincerity of the information provided, and the organization's style inform this intuition (Hensman and Sadler-Smith 2011). In some cases, a good feeling may even be perceived as a more reliable indicator than financial information (Lipshitz and Shulimovitz 2007; Hensman and Sadler-Smith 2011). It is therefore surprising not to see more relational criteria integrated into this "good feeling" in the literature. Similarly, the generally static approach of work on this topic is sometimes surprising. Indeed, according to Petersen and Rajan (2002), a feeling may evolve in the course of interactions.

At all events, the choice of lending technologies is not neutral (Trönnberg and Hemlin 2014). In the transactional model, the focus on the collection of hard information implies a loss of information, ultimately a source of competitive disadvantage (Berger and Udell 2002). Hence, we can question the basis on which financial institutions arbitrate between objective and subjective data. On the one hand, banks gain better control of behavioral risks by centralizing and harmonizing decision-making, but lose information that is useful for their competitiveness

(Petersen 2002). On the other hand, they gain informational and relational competitiveness by increasing the level of delegated authority, but see the risk of error in the advisor's decisions increase. In spite of numerous studies on the subject, research still does not yet fully understand all the intricacies in banks' decision-making. While existing studies note that a relationship is created, they fail to clarify how it subsequently evolves. Nor do they show how the bank accompanies its client throughout long-term relations, particularly in situations of difficulty. Additional work is therefore required to address the gap in knowledge on how loan officers collect information during the relationship and on the content of the relationship itself (Lehman and Neuberg 2001).

Bank Support for Small Businesses in Difficulty

The relationship involves a system of social interactions between a specific loan officer and his or her client (Lehmann and Neuberg 2001). These interactions help to inform contract specifications that are renegotiated many times in their different forms (Roberts 2015). In this context, the bank develops a better understanding of the small business environment, its needs and resources (Ennew and Binks 1995). These relations, built up over time, facilitate information transfer (Uzzi and Lancaster 2003). Since the relational dimension can help banks to identify signs of potential failure at an early date (even before they are visible in the financial data), it should also help to provide enhanced support for the client company (Bruns 2004). Indeed, this soft information can incite the banker to grant new loans, even when other indicators fail (Berger and Black 2011). Relationship lending thus mitigates credit constraints during downturns, especially for small-sized and informationally opaque companies (Beck et al. 2018). This point is essential, as we should keep in mind that failure is omnipresent and inevitable in the context of entrepreneurship (Ucbasaran et al. 2013). It is thus legitimate to wonder why such a central recurrence in corporate life has not been addressed in the literature before.

We know, however, that shocks in the relationship between loan officers and borrowers affect a bank's lending decisions, as well as the company's borrowing and repayment behavior. Drexler and Schoar (2014) show that clients are sensitive to monitoring activities by loan officers and are inclined to change banks in the event of an error on their side. Surprisingly, the other facet of this issue has not really been addressed before: how will a bank behave if a small client company suddenly faces difficulty? Will it, too, be inclined to turn to other opportunities? Bruns (2004:43) proposes a first level of understanding of the issue: "*the bank does not wait for signs of difficulties after the fact, where the borrower is unable to pay interest or installments. Instead, the bank undertakes action to limit this risk exposure ahead of time*." However, the bank-firm relationship is a more complex scenario. There are diverse degrees of support, depending on the nature of the relationship built up between the bank and the company. Thus, the question is whether a strong relationship will lead to better lending conditions, especially during critical periods (Kano et al. 2011).

In practice, trust and satisfaction play a key role in the relationship's development (Ganesan 1994). The relationship itself is decisive in the pursuit of financing in times of crisis (Bolton et al. 2013). As such, Seal (1998) shows that trust can evolve from personal interactions between loan officers and their clients, as well as more impersonal determinants such as the internal and external practices of the small businesses in question. This trust allows small businesses to negotiate optimal contracts (Roberts 2015) and thus to obtain better credit terms (Moro and Fink 2013). According to Stiglitz and Weiss (1981), trust is reinforced by actions that align the company's objectives with those of the bank. Past experience, respect for the partner's obligations, the impression of a stable relationship, and the flow of information thus help to build a shared relationship of trust and reciprocity (Lehman and Neuberg 2001; Puri et al. 2011).

However, the ins and outs of what seems here to be a relational contract (between a loan officer and his or her client) have not been studied in depth in the literature. Schoar's findings (2012) touched on this to some extent, in that she considers the relational commitment model to be bi-directional: relational support from a loan officer fosters cooperative behavior and thus reduces deviant behavior (i.e.: leaving the bank), but this would imply a relationship of loyalty developing between the two individuals (Uzzi and Lancaster 2003; Drexler and Schoar 2014). In this scenario, the loan officer adopts a proximity-based analysis of risk that is different from the view of the credit risk department, whose main purpose is to limit any impact on the bank (Bruns 2004). This could lead loan officers to take more risks to support their clients should their situation deteriorate (Whyte 1986; Staw et al. 1997). Such behavior raises the question of how, in highly structured banking organizations, bankers come to adopt the viewpoint of their clients. What are the drivers of a banker's relational commitment?

Some research provides potential explanations by showing that loan officers are part of an information analysis process, biased by affective and personal factors (Ruchala et al. 1996). In particular, they tend to underestimate risk when a relationship is longstanding (McNamara and Bromiley 1997: 1079). Thus, being responsible for a decision that has led to losses can lead to persistence and over-investment behavior (Staw et al. 1997; McNamara et al. 2002). In line with this view, Biais and Weber (2009) show that loan officers do not revise their opinion when they acquire additional information. Once an initial loan has been granted, the escalation of commitment may incite them not to inform their superiors. This escalation could even lead them to suggest that the credit committee grants additional loans, in spite of information indicating considerable risk (McNamara and Bromiley 1997; Hertzberg et al. 2010). In these circumstances, loan officers may hide negative information about the company and maintain financing until it is too late to disengage the bank (Banerjee et al. 2013). They can also manipulate the scoring systems (Brown et al. 2015) or prevent their superiors from intervening, while increasing their commitment to their clients (McNamara et al. 2002). Such an escalation will be reinforced in the event of dilution of liability, especially if a loan officer does not expect to be sanctioned in the event of a loan default (Ruchala et al. 1996; Nilsson and Öhman 2012). However, Danos et al. (1989), and subsequently Lipshitz and Shulimovitz (2007), nuance these results, showing that, under certain conditions, loan officers may call themselves into question and reconsider their positions in accordance with the additional information they obtain.

All these elements contribute to a better understanding of the mechanism of escalation in a lending decision, without actually opening the black box of the banking decisions and the relational lending scenario. While we know there is a link between escalation behavior and client relationships in banking decisions, we do not know the effects of moral or emotional commitment, or the place of peer judgment in such an escalation. For example, in the study of bank-client contractual relationships throughout the "*loan path*" (Roberts 2015: 62), the author completely ignores the psychological dimension. On the other hand, it is well known that organizational factors, such as pressure on net banking income, may conflict with socio-cognitive factors (McNamara and Bromiley 1997). Similarly, the image of the "good" professional can accentuate the situation. This image is built up by adopting behavior in line with the recommendations and expectations of superiors, in other words, the branch network and credit committee's management teams (Nilsson and Öhman 2012). Deakins and Hussain (1994) show that loan officers are more focused on the risk of approving bad funding than on rejecting good funding, which is more difficult to detect. Furthermore, they seek to project a good image of themselves to the credit committee, making it difficult for them to present their client's deteriorating situation or to explain their past decisions in this regard. The present article aims to extend these isolated reflections by seeking to understand how a bank decides to maintain – or even reinforce – its commitment to an entrepreneur when there is a risk of bankruptcy or, on the contrary, decides to terminate the credit line, marking the end of the commercial relationship.

Methodology

Given the lack of qualitative research on bank commitment (Erdogan 2018), we used the case study methodology. More precisely, we opted for a single-case approach. The latter is pertinent because it uses an in-depth analysis to reveal a phenomenon which is little known from a scientific point of view (Yin 1990).

The case chosen was that of BPro, a mutual bank that has belonged to France's second-largest banking group since 2009. Its development on the market of small and large companies is quite recent (late 1980s). This financial institution is divided into 17 independent regions, each comprising an average of about 250 branches, and each regional bank is divided into sectors, groups and branches. In this study, we focus on a single region and examine BProAq (2,800 employees and 375 branches).

Within BproAq, we focus on the retail banking business, especially the small business market (craftspeople, small retailers and independent professionals). This gives us insights into the particular case of entrepreneurs in difficulty. Large companies were excluded from our analysis. Our focus is on the behavior of the bank with respect to entrepreneurs that are already part of the small-business advisors' (SBA) client portfolio and whose financial health is deteriorating. This has been likened to an "exogenous shock" (Drexler and Schoar 2014: 2722), exposing the bank to a risk of bankruptcy.

Monitoring the way clients' situations evolve is part of the SBAs' mission.[2] Generally, SBAs are therefore the preferred entry point for requests for overdraft facilities, credit lines or bank

[2] As a loan officer, an SBA manages a portfolio of 100 to 200 small or very small companies whose turnover does not generally exceed €4 million.

loans when an entrepreneur is in difficulty. However, depending on the bank's delegation policy, the final decision does not necessarily come from the SBAs, and may be incumbent upon their superiors (e.g.: branch director, group director, sector director, credit committee, debt-collection service, litigation service) when the bank's exposure level is high.

Data Collection and Analysis

Between February and June 2017, we contacted the main internal stakeholders at headquarter and network levels, who intervene when a decision to pursue or abandon a commercial relationship with a struggling entrepreneur is made. We interviewed 22 people by way of semi-structured and systematically recorded interviews, each lasting one hour on average.[3] The interview guide was divided into four sections: procedures for entrepreneurs facing the risk of bankruptcy, support for entrepreneurs in difficulty, subjectivity of the decision, and examples of concrete cases. The interviews ended when we reached data saturation (Yin 1990). Once transcribed, our interviews gave a raw data corpus of 319 pages. In addition, we collected all procedures relating to the delegation policy of BproAq for the small business market. This documentation details the level of delegation according to criteria such as the entrepreneurs' Basel II rating, total gross outstanding, and type of sector.

In order to process our data, we used the methodology of Gioia et al. (2013). In this approach, first-order coding faithfully reproduces the respondents' discourse, ignoring the literature. Thus, a first reading of the collected data allowed us to generate items for each new idea detected (30 in total). The second-order coding is designed to aggregate these items through

[3] At the Head Office, we interviewed: 1 director of commitments, 1 director of the litigation service, 1 head of special affairs (attached to the debt collection service), 1 director of internal audits (former member of the executive board), 1 analyst (attached to the direction of commitments) and 1 jurist. Within the network, we interviewed: 1 sector director, 4 Risk and Internal Controls Advisers (reporting to a sector director), 1 director of the small business market, 1 commercial organizer for the small business market, 2 group directors, 3 branch directors and 4 SBAs.

two successive levels of abstraction, moving back and forth between the raw data and the literature. For instance, a notion such as affective bias comes from the literature, whereas the interpretation of difficulties is an emerging concept. Table 1 below shows how we ultimately progressed from 30 first-order codes to 12 second-order themes, and then to 6 aggregate second-order dimensions.

[Table 1 near here]

Once our 'Gioia grid' was created, we coded all the data collected. This allowed us to build a 127-page file with quotations (classified according to the data structure in Table 1), from which the empirical results were then written. The corresponding section of our manuscript is structured according to our aggregated 2nd-order codes, given that all the terms appearing in italics are taken from our respondents. Ultimately, this approach enabled us to generate a conceptual model of bank commitment to entrepreneurs in difficulty (see Figure 1).

[Figure 1 near here]

Empirical Results

Difficulty Alert

BPro has different alert systems at its disposal to identify entrepreneurs in difficulty. First, entrepreneurs sometimes take the initiative to inform the SBA of their problems (e.g.: unpaid invoice(s), loss of a significant contract), or even solicit the loan officer for support (e.g.: overdraft facilities, credit lines). This gives the latter the opportunity to carefully study the client's file and to take note of the deteriorating situation. However, such proactive behavior by the entrepreneur remains exceptional.

Nevertheless, as part of the regular monitoring of their clients in the portfolio, SBAs analyze their clients' balance sheet and income statement, as well as how their bank account is functioning. In the event of negative cash positions and/or financial losses, SBAs will not hesitate to call the clients concerned to obtain additional information about their situation. At all events, in accordance with the “relationship contract” signed with each entrepreneur, at least one appointment a year is planned with the client after the annual accounting documents are produced. This is when the SBAs conduct a “full review” of the company's situation (e.g.: activity, margins, financial structure, bank loans). More generally, loan officers have monitoring tables and financial indicators to identify any irregularities in the businesses they support “very early on”. In addition, SBAs can also use available sector data to compare their client's financial results with the market average (e.g.: commercial margin, EBITDA[4], net income).

Moreover, banks have automatic warning systems to identify entrepreneurs in difficulty. In particular, each business owner has a Basel II rating. This rating is calculated monthly according to regulatory criteria, decreases as a company's financial situation deteriorates (e.g.: debit balance, exceeding overdraft limit, unpaid loan, check rejection), and is accessible to all bankers. Each morning, they also have a list (called MAD) containing the “pending transactions” they need to validate or reject (e.g.: payment of a check to a supplier despite a debit balance). The regular presence of an entrepreneur on the MAD thus constitutes a warning signal for the banker. Additionally, the bank has a second type of file (called an RPM), designed to detect the “potential major risks” of cessation of payments.[5]

Finally, SBAs also pay close attention to negative signals arising from the entrepreneur's private life (e.g.: high salary, expensive lifestyle, divorce, changes in assets). These signals are sometimes an early sign of difficulties in the company management.

[4] Earnings before interest, taxes, depreciation, and amortization.

[5] MAD = *Mouvements en Attente de Décision* (literally, transactions waiting for decision). RPM = *Risques Potentiels Majeurs* (literally, major potential risks).

Activity Framework

The use of systems to detect struggling entrepreneurs is in line with the logic of compliance with banking standards. Indeed, BPro's lending is governed by a series of prudential regulations that influence its risk policy. For example, a fall in an entrepreneur's Basel II rating must lead to a provision for risks in accordance with the minimum capital requirement of the Basel II accord. Similarly, this rating determines delegation within the bank. As such, it limits the scope of SBAs' intervention in the management of entrepreneurs in difficulty. This external environment explains the recent emergence of Risk and Internal Control Advisors (RICA),[6] responsible for ensuring compliance with this very strict regulatory framework. In practice, the framework certainly helps to strengthen the soundness of credit institutions, but its constraining nature also explains banks' lack of appetite for "at-risk clients" such as entrepreneurs likely to go bankrupt.

Moreover, banks do not have full liberty in their support of this type of company. In particular, they may be sued for "abusive support" if they keep a company alive artificially to save outstanding bank loans. Conversely, the bank may also be sued for "wrongful termination". Indeed, according to the law, relations can only be interrupted if the company's situation is "irremediably compromised". In addition to the "credit risk", there is thus a "legal risk", which also influences bank commitment.

Beyond this regulatory compliance imperative, and owing to its status as a mutual bank, BPro also seeks to adopt socially responsible behavior towards its customers. Hence, the financial institution does its utmost to avoid terminating bank credit facilities (which almost invariably leads to bankruptcy) and seeks to go "as far as possible" in its commitment. The bank actually considers that it has a "moral obligation to try to find solutions". "Supporting an

[6] RICAs are typically highly experienced (e.g.: former branch directors).

entrepreneur in difficulty" is even considered by several SBAs as the noblest part of their job. However, the loan officer's role is also to avoid any form of escalation on the part of struggling entrepreneurs.

Commercial Logic

SBAs face a paradoxical decision. On the one hand they avoid "at-risk customers" and, on the other, they lend support to entrepreneurs in difficulty "as far as possible". Consequently, they manage the tension between these two perspectives by being very vigilant when entering into a business relationship. Indeed, loan officers are extremely cautious when they grant a bank credit line to avoid any future difficulties as far as possible. The SBAs at BPro no longer look to "do business" at all costs. They are more than ready to refuse to open an account or to fund a request if a business venture does not appear viable and/or if the 'feeling' with the customer is not good. SBAs are thus very selective, to such an extent that there is now "much less damage" (in other words, bankruptcies) among entrepreneurs.

Moreover, at the very beginning of the relationship, a moral contract is concluded with the entrepreneur with a view to establishing "reciprocal trust" between the two partners. This allows SBAs to define a very precise framework in which they wish to collaborate, underscoring values such as transparency and honesty. The SBAs explain precisely what they expect from a client (e.g.: regular updates about their situation, not "putting the banker up against the wall" in the event of complications).

Under this "good relationship contract", loan officers will be more inclined to remain committed until the end with an entrepreneur whose situation deteriorates, as long as the latter "plays the game". Indeed, they know that if they "do not drop" a struggling entrepreneur, the latter will feel grateful if the company recovers, resulting in greater trust, increased loyalty, and word-of-mouth referrals. Bankers in branches are aware that conquering new customers is difficult in a saturated market and that building a business relationship takes time. It is therefore not in their best interest to exclude entrepreneurs in difficulty if they wish to continue to develop their portfolio. As such, SBAs clearly assume that "taking risks" – here, continuing the relationship – is an integral part of their job. At head offices, this attitude of sometimes excessive support for clients can be seen as a tendency to get "locked in", reflecting an absence of "risk culture". In this respect, it should be stressed that loan officers do not receive specific training on managing such complex affairs, which remain relatively rare at their level and require specific skills. On a day-to-day basis, SBAs are primarily focused on "doing business".

Beyond the desire to satisfy clients, maintaining SBAs' commitment to an entrepreneur in difficulty also involves an affective dimension, as the commercial relationship with an entrepreneur is often built up over time. Given this "closer relationship", SBAs tend to become attached to "my account" or even "my client". Loan officers may consequently lack the objectivity needed, no longer involved solely in the technical analysis of the case, but also taking a (partially) emotional approach to things; in this sense, they are more subjective. Even though SBAs are aware they should not "include feelings" in their decisions, some of them may nevertheless be sensitive to the financial and psychological difficulties faced by an entrepreneur, who has often invested personal money (e.g.: risks losing assets, impact on family life). Being "affected" by the client's situation may explain why some SBAs do not want to "drop" them, sometimes at the risk of endangering the bank (e.g.: giving unjustified overdraft authorizations), which could be perceived as misconduct by their superiors).

In the same vein, SBAs may tend to overemphasize the positive aspects of a situation with their line managers (when they are no longer delegated to manage the case), systematically siding with the client and putting themselves in the position of "defender" of the entrepreneur. They will generally build an argument to support the dossier, "smoothing things over", even if this means sending several reminders to the management to find a solution that will satisfy their client. As a result of this "close relationship" between the banker and the entrepreneur, most SBAs take it badly if they are removed from an at-risk case because of the procedures relating to delegation policy. This is all the more "hurtful" for them in that they generally perceive it as a commercial failure (e.g.: it could be interpreted by their superiors as an error in the account selection process, with a drop in the branch's loss ratio).

Risk Logic

To counterbalance this commercial and sometimes emotional response, BPro can provide financial experts (e.g.: RICA) and legal experts. In case of doubt, SBAs are encouraged to turn to the latter for a risk assessment of maintaining their commitment to an entrepreneur in difficulty or, on the contrary, terminating the bank credit lines. Except in rare cases, these experts do not have direct contact with the clients (so as to avert the potential for empathy) and focus solely on analyzing the case to obtain the most objective view possible of the situation. In other words, their opinion is based on "tangible elements" and is not influenced by the client. Above all, they seek to respect the delegation chain and the bank's risk policy.

For example, RICAs do not have a client portfolio. Since they are more accustomed to dealing with complex cases than SBAs, they play a supporting role for loan officers. They are there to give a well-argued and reasoned opinion of the company in difficulty's financial situation and to propose potential solutions. In practice, their recommendations are often "very cautious". This "fresh outlook" nonetheless prevents SBAs from becoming isolated, and allows them to take a step back from their most sensitive cases. In addition, RICAs are also tasked with determining whether an account submitted by a branch – in the event that the branch considers the situation too complex, detects a risk, or wishes to terminate the bank credit line – should switch to the debt-collection service at the head office. Conversely, if the commitments department (in charge of risk monitoring at the head office) identifies an abnormal situation with a client in a branch, the RICAs will be asked to approach the branch in question to help the SBA settle the situation.

Moreover, in certain situations deemed particularly bad (e.g.: over 60 days of unpaid loan, over 60 days of unauthorized overdraft, entrepreneur's Basel II rating equal to or greater than 10, total gross outstanding above certain predefined thresholds), BPro's procedures stipulate that the branch must be automatically removed from the case in question. More specifically, the dossier is transferred to the debt-collection service for a counter-analysis and presentation to the credit committee. This collegial body, chaired by a member of the Executive Board, reasons mainly in terms of financial and legal risk management. In particular, it assesses whether the situation is likely to lead to a cessation of payments.

In the event of a favorable opinion from the credit committee, the debt-collection service is then responsible for managing the account in order to try to find solutions with the entrepreneur. For their part, the SBAs no longer intervene at all in the relationship. Their role is limited to completing a "transmission form" concerning the client, addressed to their colleague at the head office (e.g.: assessment of the company's situation, summary of decisions taken, reasoned opinion). In particular, the debt-collection service advisors must take all decisions regarding the granting of new loans or accepting additional payments despite a debit balance. In this way, the bank seeks to redress the company's situation before it is "irremediably compromised" and thereby reduces its financial risk and exposure regarding outstanding amounts.

Even though the debt-collection service interacts with the client over time, this relationship is essentially remote. What is more, there is no longer any shared history or affective proximity between the banker and the entrepreneur. Hence the exchange is not biased by subjective considerations. Indeed, the banker tries to be "as cold as possible" to "make the decision as objectively as possible" through a "vision driven by figures". In addition, with a smaller client portfolio than an SBA, advisors at the head office can devote more time to each case. In this way, they can often put “more pressure” on entrepreneurs to reduce their overdraft and repay their loans.

In practice, most of the accompanying measures do in fact lead to debt repayment plans, after which the client can – after a period of observation – return to the branch if the business progresses favorably. On the other hand, if the venture is not deemed viable by the credit committee or if the entrepreneur is unable to resolve his or her cash flow problems despite the repayment plan (e.g.: the client goes bankrupt), the case is forwarded to the litigation service. In this case, the management will be even “less flexible” with, here too, a “risk perspective” aimed essentially at recovering the sums due to BPro.

Interpretation of Difficulty

As well as arbitration between the business/affective logic and the risk logic, maintaining the bank’s commitment or not also depends on the banker's interpretation of the entrepreneur's difficulties. In practice, as soon as SBAs detect an irregularity, they contact the client for an explanation. In such cases, the loan officer seeks to understand “the origin of the difficulties”. This diagnosis of the situation aims to determine whether the manager's problems are short-term (e.g.: extraordinary climatic event, fire on the premises, late payment by a key account client, sector in crisis) or structural (e.g.: business issues, commercial mismanagement, obsolete product, over-consumption of capital, entrepreneur’s salary too high, too many employees). If, on reading the accounting documents and the information provided, loan officers consider the client's troubles to be only temporary (e.g.: cash flow timing differences), their confidence in the venture is not affected.

In fact, SBAs look to obtain reassuring prospects for the future by way of written evidence (e.g.: accepted cost estimate, invoices issued, worksites or orders in progress). SBAs are also attentive to solutions proposed by their clients to “get out of the rut” (e.g.: actions undertaken to fill the order book) and expect a “watertight” business plan. If bankers are ultimately convinced that the situation is not “irremediably compromised” and is unlikely to lead to other unpaid debt or overdrafts, they will do their utmost to accompany their client through new bank credit facilities, for instance.

Pursuit of the business relationship is driven by the SBA's confidence in the individual client as well as the company's chances of bouncing back. In particular, although loan officers unanimously claim that they “never do business just because of a guarantee”, if such financial security has value (e.g.: real estate mortgage), they will certainly feel “more comfortable”, allowing them to “go a little further” in the support they give. The guarantee is thus a means of “sharing the risk” with the entrepreneur in a two-way rapport.

At the same time, the entrepreneur’s behavior is also decisive in the decision to maintain (or not) the bank’s commitment if the company’s situation deteriorates. In accordance with the “relationship contract”, the entrepreneur’s “good faith” and the “quality of the relationship” are fundamental criteria for SBAs. As such, several factors are considered as unacceptable by branch-based bankers. These include cases where clients refuse to face reality, are not transparent about their situation, hide information, do not keep promises, do not send their accounts in due time, do not respond to requests, get annoyed when contacted, do not call themselves into question, do not listen to advice, and so on. Thus, SMAs will generally be inclined to drop a client by terminating bank credit lines or forwarding the dossier to the debt-collection service, for example, should entrepreneurs “lock into their problems”, become “evasive”, “bury their head in the sand” or “try to fool the banker”. In effect, SBAs seek to “work in a trusting environment” within the framework of a partnership. On the other hand, entrepreneurs who are proactive – that is, who spontaneously go to see the banker upstream to set out their problems and find a solution – or, quite simply, who “put their cards on the table” and “play the game” will be supported far more readily.

Support for Struggling Entrepreneurs

Once SBAs decide to support an entrepreneur in difficulty, the measures can take two distinct forms. First, loan officers draw on their experience (of similar cases) to play an “educational” and advisory role. First, they identify “matters for attention” (e.g.: insufficient margin, out-of-sync forecasts) to make an entrepreneur aware of the situation. Second, they help the clients to find concrete solutions (e.g.: inventory or invoice management, reduction of certain expenses, work organization, opening up capital, replacement of worn equipment for greater productivity, sale of real estate). However, SBAs are careful not to attempt to replace the chartered accountant and not to “interfere” in the company’s management. In other words, bankers only make suggestions to “guide the client”, and the latter remains free to apply the advice or not. In practice, defining the “limits” in terms of advice varies considerably from one loan officer to another. For example, some SBAs refuse to give their opinion on a client's business strategy, while other colleagues will not hesitate to suggest potential market opportunities, changes in sales prices, or changes in opening times.

In addition, loan officers can also suggest new banking products to the entrepreneurs to help them overcome their difficulties. In particular, faced with a problem of cash flow timing difference, SBAs have various short-term financial solutions available (e.g.: liquidity line, factoring, daily assignment, additional overdraft authorization, promissory note, bank discount) on which they can give advice. Similarly, with a new medium/long-term loan aimed at strengthening equity capital, SBAs can help their clients define the amount they need, as well as the repayment terms. In the same vein, they can suggest other commercial solutions, such as refinancing a recently self-financed investment or credit smoothing when the reimbursement costs are too high.

Discussion

Determining Factors for Maintaining Bank Commitment

Figure 1 represents the main theoretical contribution of our research. This model serves to establish that two distinct processes are involved when banks have to make a decision to maintain (or not) their commitment to struggling entrepreneurs, and to accompany them despite the difficulties detected by the alert systems. The first involves arbitration between two opposing modes of reasoning: the business logic (at the level of the loan officer) and the logic of risk (at the level of the latter's superiors in the delegation chain). Such arbitration takes the social ethics and conformity requirements attached to the bank's activity framework into account. The second process refers to a sensemaking approach, highlighting the importance of the banker's interpretation of the entrepreneurial difficulty (Weick 1995).

The Tension Between Business Logic and Risk Logic

The contrast between the two approaches (business vs. risk) proposed in this paper complements the traditional opposition between relational and transactional models, criticized by Berger and Udell (2006). Following these authors, we show that the commercial logic is specific to the close relationship between loan officers and their small business client. This logic is informed by specific subjective elements of appreciation (soft information based on impressions). Conversely, we show that the logic of risk relies solely on an objective analysis of financial indicators (hard information centered on figures). It deliberately encourages the development of distance (geographical and relational) from the entrepreneur.

On the last point, our research confirms that the organizational factors (here, the role of the RICAs, the credit committee or the debt-collection service, for example) are mainly designed to control emotional bias (McNamara and Bromiley 1997; McNamara et al. 2002). This conclusion underscores the need for reasoning in terms of complementarity and the articulation of both these financing models for the organization, rather than cleavage (Berger and Udell 2006). In this particular case, loan officers try to develop the bank's business (seeking to build customer loyalty by offering new banking products), while the distant hierarchy is primarily concerned with reducing the risks caused by the entrepreneur’s financial troubles (seeking to recover the debts due or to limit losses), excluding any potential for empathy.

In this respect, the organization’s implementation of mechanisms and procedures (e.g.: scoring, listing risky clients, delegation policy, RICAs and support experts) to prevent loan officers from being too isolated when one of their small business clients’ financial situation is deteriorating, emerges as an important finding from this research. Indeed, it is likely to prevent any sort of escalation of the bank’s commitment in the form of a succession of commercial solutions (Biais and Weber 2009; McNamara et al. 2002), which may develop net banking income but are ultimately likely to backfire on the bank if the client company fails to repay its debts.

However, the main theoretical contribution in connection with the arbitrage between two distinct logics (business vs. risk) hinges on a dynamic interpretation of such a phenomenon. The literature traditionally considers that banks base their lending decisions on either one of the two financing models (transactional or relational), or on a combination of both models (Berger and Udell 2006). However, we show here that the bank’s choices are not fixed but can evolve according to the supported company’s financial results. Thus, a small business can seamlessly switch from the branch to the head offices, and then back from the head offices to the branch again, depending on whether the situation degenerates or, on the contrary, improves. The firm’s results can thus be interpreted as “exogenous shocks” (Drexler and Schoar 2014: 2722) that modify the lending technologies. In this particular case, the approach will be transactional only when a small business is in poor health, and will become more relational as soon as it recovers.

The idea of oscillation between the two financing models over time is consequently another theoretical result of our research.

Sensemaking by the Small Business Advisor as a Soft Information Production Tool

The balance to be found between a business and a risk logic over time does not, in itself, explain why banks maintain their commitment to an entrepreneur in difficulty or not. The loan officer's sensemaking (Weick 1995) plays an equally important role. When a small business registered in the customer base is in difficulty, it should be remembered that this alters the loan officer's traditional points of reference since it is a relatively singular situation in the latter's everyday life. The fact that financial indicators are downgraded creates strong uncertainty around the business, yet opaque and risky financing requires discretionary decisions (Cerqueiro et al. 2011). According to Puri et al. (2011), a loan officer's discretion is normally based on soft information for clients with no credit history and hard information for clients with a credit history. This assertion is partially called into question in the specific context of struggling entrepreneurs. We show that when a small business is in trouble, loan officers are no longer able to base their decisions on formal and tangible criteria (the financial indicators they usually trust are inadequate when the company is in difficulty) and so their judgment is broadly based on intuition. This finding is consistent with Greifeneder et al. (2011), according to whom bankers' decisions tend to be based on intuition in uncertain cases. Thus, in the banker's decision-making framework, we observe a shift from the bank perspective (e.g.: which rules apply?) to the business organization perspective (e.g.: what are its chances of survival?).

In practice, loan officers' intuition arises from the meaning they give to the difficulties faced by an entrepreneur, depending on whether they consider the origin of the problem as short-term or structural in the light of the explanations provided by the client. This diagnosis is fundamental because any difficulties that arise in an entrepreneurial venture totally modify the analysis made before entering into the relationship. In addition, the bankers' intuition is also based on extended interactions with the entrepreneur (Berger and Black 2011; Lehman and Neuberg 2001). This intuition gives them a pretty clear mental representation of their customer's behavior if a situation worsens (e.g.: honesty, listening, transparency, questioning). If the customer has a positive attitude despite the problems encountered, the loan officer will get a "good feeling" (Lipshitz and Shulimovitz 2007; Hensman and Sadler-Smith 2011) and vice versa.

Finally, it appears that on the basis of soft information, loan officers are potentially able to revise their opinion when they acquire hard information that indicates a weakening of the company's financial situation (e.g.: Basel II rating downgraded). In this case, if the client does not present reassuring prospects for the future (the difficulties appear *a priori* structural) and/or he or she is dishonest (does not honor commitments to the banker), a loan officer will not hesitate to terminate the bank credit line. This capacity of loan officers to call themselves into question therefore contradicts the conclusions of studies on escalation of bankers' commitment (McNamara et al. 2002; Biais and Weber 2009). Our analysis instead ties in with both Danos et al. (1989) and Lipshitz and Shulimovitz (2007); according to these authors, loan officers are able to reconsider their positions depending on the additional information they obtain. One of the main interests of our article is thus its specification of the nature of this additional information. More precisely, our research affords a better understanding of the role of soft information (Uchida et al. 2012) when supporting a small business client in difficulty. In this particular case, the logic of sensemaking (Weick 1995) and the ensuing confidence in the business venture and in the entrepreneur as an individual (Bolton et al. 2013; Ganesan 1994) inform the subjective intelligence of the loan officer (Stein 2002; Uchida et al. 2012). As we said earlier, the bank will thus have to arbitrate between mobilizing this soft information to take a conscious decision (discretion) or limit its risks (rule) (Cerqueiro et al. 2011).

Towards an Enrichment of the Relational Lending Model

Subjective information plays an important role in the support afforded to small businesses (Bruns et al. 2008). It is even crucial, as we have just seen, in the case of lending decisions made for small businesses in difficulty, and can go hand in hand with behavioral bias in the decision-making process. The existence of these cognitive and affective dimensions – sources of bias – has often been emphasized in the literature on banks' decisions (Behr et al. 2011; Ruchala et al. 1996). In a classical way, our research shows how physical and relational closeness with the client influences the judgment made by loan officers (Petersen and Rajan 2002; Petersen 2004). However, we also note that this is particularly true in the small business segment, since commercial relationships are generally established over the medium to long term and consequently give rise to a number of interactions over time (Berger and Black 2011; Drexler and Schoar 2014). Moreover, we highlight some new elements that may explain these emotional biases. In our particular case, we show that loan officers are often sensitive to the repercussions of financial difficulties on an entrepreneur's psychological and family situation (Ucbasaran et al. 2013). This empathy may subsequently distort their understanding of the situation.

In addition, our study introduces the new concept of a psychological contract (Rousseau 1989) in the bank commitment process, which supplements existing work on the bank-client contractual relationship (Roberts 2015). Our paper actually reveals mutual obligations that bind bankers and their clients once the relationship has been established. Such a contract favors the production of soft information in particular. More precisely, we show that loan officers generally feel morally committed to their small business clients as long as the clients "play the game" and honor their initial commitments (e.g.: are responsive, communicate). Providing the relationship of trust is maintained, loan officers will do their utmost to honor their own commitment and support the struggling entrepreneur, to the extent of playing the role of the entrepreneur's "defender" with their superiors (Ruchala et al. 1996; Nilsson and Öhman 2012). In other words, our study puts forward an ethical interpretation of bank commitment at the level of network branches. From this perspective, "good professionals" are no longer merely officers who stick to their superiors' recommendations and expectations (Nilsson and Öhman 2012) but will also help entrepreneurs to cope with their difficulties. We suggest that such a reasoning model can distort loan officers' diagnosis of the situation as they inevitably become more accommodating in their analysis of the business's chances of rebounding. Consequently, loan officers face a conflict of loyalty between, on the one hand, their desire to respect the bank's rules and, on the other, honoring their moral commitment to the client.

In short, our research offers a kind of reincarnation of loan officers, highlighting new elements in their decision-making process. In particular, we suggest the integration of their free will (e.g.: definition of limits in terms of advice for each officer), feelings (e.g.: empathy for the distressed client), morality (e.g.: psychological contract), internal conflict (e.g.: ethical dilemma between bank's interest and loyal client), and multiple interactions within the organization (e.g.: negotiations with superiors). However, loan officers are still very much influenced by their business and working environments. In this respect, our paper questions the idea that loan officers may not inform their superiors that the client is encountering difficulty (Hertzberg et al. 2010). Indeed, the weight of compliance with banking standards in lending commitment today makes this type of situation far less plausible. In practice, the risk has been counteracted by the automation of alert systems, with both upward (from the branch to head office) and downward (from head office to the branch) movement of information.

Conclusion

Starting from the observation that most research work on bank commitment is highly static, we opted for a dynamic interpretation of this phenomenon, examining the behavior of financial institutions when confronted with a small business already in the client portfolio that faces financial difficulty. We attempted to understand how the bank reacts to this exogenous shock (Drexler and Schoar 2014) and what elements underpin its decision to terminate, maintain or even reinforce its commitment to an entrepreneur in difficulty. To answer this question, we conducted a qualitative study of a French retail bank.

Using the methodology of Gioia et al. (2013), we developed a theoretical model of how bank commitment to a struggling entrepreneur is maintained. First of all, the model highlights an oscillation and arbitrage, over time, between a business-related logic and a risk-related logic. It then underscores the importance of ‘feeling’ for the loan officer. This feeling depends on the meaning an officer gives to (1) the entrepreneur's financial difficulties and (2) the entrepreneur’s attitude as a manager (skills) and as a client (good faith). Moreover, our study also considerably enriches the relational lending model, introducing the concept of a psychological contract between loan officers and their clients, for example.

From a managerial point of view, this paper allows us to envisage a solution of more personalized banking support for entrepreneurs in difficulty. In addition, the article is useful for small businesses whose financial situation is deteriorating. Indeed, they often have difficulty knowing how to behave with their banking partner. We pinpoint some key factors that may reassure (or, on the contrary, worry) a loan officer in such circumstances.

All these remarks must, however, be put into perspective with one of the limitations of this research, namely the very singular context of a mutualist bank, which inevitably limits the external validity of our results. As such, a future research avenue could consist of opting for an experimental methodology by drawing up a scenario of a small business in difficulty, which we would then submit to various French (or European) banks in order to identify the model of reasoning specific to other financial institutions.

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Table 1
Data Structure Following the Methodology of Gioia et al. (2013)

First-Order Coding	Second-Order Coding	Aggregated Second-Order Coding
‘*The warning signal will firstly be the analysis of a balance sheet. Maybe an account operation.*’	Professional alert	Difficulty alert
‘*We have automatic alerts for payments incidents (...). We have a listing that comes out every day, on which we have the pending transactions. This is our first alert.’*		
‘*If I see him or her driving a BMW, I’ll look at the balance sheet (...). We have to be attentive to everything that happens in the client’s everyday life.’*	Private alert	
‘*If you have downgraded ratings, equity capital allocations are subjected to relatively large consequences.’*	Conformity	Activity framework
‘*When a company is artificially kept alive, the law determines it as a situation of abusive support.*’		
‘*We have to act as safeguards and tell the client: "Listen, no, stop! ". We have to stop before the situation becomes difficult for him or her and for us.*’	Social ethics	
‘*Support for entrepreneurs in difficulty is the best way to show that we’re a socially responsible company.*’		
‘*Great care is taken before entering into a relationship to avoid this kind of situation.*’	Business development	Commercial logic
‘*When I meet someone, I define the framework in which I want the relationship to unfold.*’		
‘*We have a commercial approach (trying to maintain the relationship, develop it), while limiting the risk. The RICA mostly has a risk perspective.*’		
‘*Salespeople are not ready and are not trained to deal with entrepreneurs in difficulty. That’s not what they‘re asked to do.*’		
‘*It’s very difficult to eliminate any emotional input from the dossier.*’	Affective bias	
‘*The SBA will try to place maximum emphasis on the positive aspects of the situation and to be the best possible advocate for the client with the credit committee, in order to get through the difficult time.’*		
‘*We have some SBAs that may have somewhat intense reactions (...). Is it a small failure on their part that their client is in litigation? Yes, possibly.*’		
‘*We call the legal department and we have people who answer us.*’	Risk advice	Risk logic
‘*At sector level, we have two experts in risk analysis. We turn to those people when we have a doubt.’*		
‘*We have a more objective vision, driven by figures. We don’t have influence over clients that we could grant bank loans or overdrafts to because they’re nice or because they make a good impression.*’		
‘*The amount of outstanding bank loans or the rating means that, at some point, the dossier leaves the branch's delegation to go back to head office.*’	Delegation of risk	
‘*I sometimes said: "Listen, with this client, for various reasons, I can’t do it anymore!" Because there may also be relational problems at some point.*’		
‘*We have a transmission form to fill out explaining the origins of the client’s difficulties. It’s signed by the SBA, the branch director, and is then forwarded to the debt-collection service.*’		
‘*We take the dossier out so that the SBA doesn’t feel responsible. So that the affective and close relationship that’s been created between an SBA and the client disappears.*’		
‘*Basically, the purpose of this diagnosis is to distinguish between two things: are the difficulties structural or short-term?’*	Project trust	Interpretation of difficulty
‘*We need to have a global vision of what will happen.*’		
‘*We don’t do business just because there’s a guarantee. But if the security has value (e.g.: if the person is the owner) and if I believe in the project, I would be more comfortable. It has an influence.*’	Individual trust	
‘*If we no longer have this partner relationship, if the client talks nonsense, or if nothing is precise in his or her discourse, we can’t work with confidence or support the entrepreneur in difficulty.*’		
‘*The more experience we’ve gained and the more we’ve dealt with all kinds of business (...), the better we’re able to educate the client.*’	Advice to the client	Support for the struggling entrepreneur
‘*The bank can give all the advice it wants, provided it doesn’t interfere.*’		
‘*In the short term, we can fall back on factoring, daily assignment, a better dimensioned overdraft, a promissory note, and so on.*’	Banking techniques	
‘*The debt-collection service can propose short term credit, but most of the time it introduces settlement plans.*’		
‘*At the litigation service, apart from judicial redress, we’re not really geared toward support.*’		