

<http://researchcommons.waikato.ac.nz/>

## **Research Commons at the University of Waikato**

### **Copyright Statement:**

The digital copy of this thesis is protected by the Copyright Act 1994 (New Zealand).

The thesis may be consulted by you, provided you comply with the provisions of the Act and the following conditions of use:

- Any use you make of these documents or images must be for research or private study purposes only, and you may not make them available to any other person.
- Authors control the copyright of their thesis. You will recognise the author's right to be identified as the author of the thesis, and due acknowledgement will be made to the author where appropriate.
- You will obtain the author's permission before publishing any material from the thesis.

An analysis of the benefits for New Zealand banks  
of adopting a relationship banking model for small  
business clients.

A thesis

submitted in fulfilment

of the requirements for the degree

of

**Doctor of Philosophy**

at

**The University of Waikato**

by

**Zakaria Boulanouar**



THE UNIVERSITY OF  
**WAIKATO**  
*Te Whare Wānanga o Waikato*

**2013**

## Abstract

This thesis provides a discussion of research into the sources of value creation and addition accruing to banks through the use of relationship banking with small business clients. The investigation involves business managers in several banks and accordingly it portrays their perspective. The study addresses four key questions: (i) what does relationship-banking mean to the five major bank brands in New Zealand? (ii) How does the relationship-banking process actually work? (iii) What are the sources of value (i.e. benefits) of relationship banking to these five major bank brands when dealing with small businesses, and, (iv) how do these banks secure the benefits?

Prior research into relationship banking and small business has concentrated on the potential benefits to the businesses. The literature contains both normative theorising and empirical work addressing aspects of the relationship and the benefits accruing to the small business. What is not supported by prior research is an understanding of why the banks engage in relationship management processes with small business. The obvious answer is that it is profitable. This in turn begs the questions of returns and risks faced by the banks and how these are managed.

The nature of the research questions which are about investigating processes suggests the use of a qualitative research approach. A multiple case study approach points the research method toward conducting interviews with relationship managers, selected using theoretical

sampling, from the five main bank brands and across the five metropolitan cities in New Zealand. The big five control 85% of the registered banks' total assets in New Zealand and dominate the small business market. The primary data collected through interviews are analysed using the thematic analysis method.

This research produces a number of key findings which directly address the research questions and go beyond. It is found that the working definition of relationship banking departs from that often quoted in the literature in a number of ways. This supports the contention that banks use relationship banking as an overarching approach, within which other lending technologies may be employed with their small business clients. Sources of value creation and addition stemming from relationship banking for the banks are clearly identified. In addition the processes and mechanisms by which banks operationalise and secure these benefits are revealed. How new relationship banking benefits are identified, creating and adding value to banks are traced through the interviews. The findings around these new benefits have important implications for the current research in regard to comparative studies of the different lending technologies in general and more specifically to the future of relationship banking which is challenged by an increasingly competitive financial markets.

From an understanding of how bank relationship managers perceive the dynamics of their roles in creating relationship banking benefits a risk-

return taxonomy is formulated. Issues emerging from this formulation/taxonomisation relate (i) practically, illustrating how these taxonomies can benefit banks, such as helping banks identify when to expect each benefit and to develop best practices (e.g. training staff and providing infrastructures), consequently ensuring the maximisation of the scooping up of all possible relationship banking benefits. Thus improving banks' performance in terms of risk mitigation and increasing return. (ii) Conceptually, the thesis shows how the risk-return taxonomy, for example, can help in defining and positioning relationship banking at the heart of the banks' decision making in regard to small business.

The thesis contributes to the small business finance knowledge base in several ways. There is a clear identification of both the different types and different levels of relationship banking, depending on the criteria used by banks to silo businesses into online, small business, or medium business relationship banking models. The non-uniform, but definite similarities, between banks does indicate the contextual nature of the issues. The banks' approach to retention is noteworthy and their respective investment into discouraging a small business from changing banks provides an insightful juxtaposition to prior research investigating the benefits and costs of changing banks.

The thesis findings offer several opportunities for future research. One such example of a research agenda relating to the different levels of relationship banking discussed above is the modelling of the three

different levels of relationship banking. This could utilise, for example, a piecewise type of function which could then be followed by an empirical study to test and measure the accuracy of the model. It would also serve to test the claims made in this thesis regarding the identification of both the different types and the different levels of relationship banking.

## Table of contents

Abstract .....	2
Table of contents .....	6
List of figures .....	11
List of tables .....	12
I. Introduction .....	13
I.1 Background to the research: .....	13
I.2 Gap identification and motivation for the study .....	14
I.3 Research problem, propositions, uniqueness and importance of the study: ...	17
I.3.1 Research problem: .....	17
I.3.2 Research questions: .....	18
I.3.3 Uniqueness of the study: .....	18
I.3.4 Contribution and importance of the study .....	20
I.4 No human endeavour is perfect: scope and limitations of the study: .....	25
I.5 Thesis organisation .....	25
II. The framework of the study .....	27
Introduction .....	27
II.1 Prior research about SMEs and banking: .....	27
II.2 SME finance: .....	33
II.2.1 Information asymmetry and SME finance .....	36
II.3 Challenges and issues for banks when dealing with SMEs: .....	39
II.3.1 Opacity: .....	40
II.3.2 Information Asymmetry .....	42
II.3.3 Size of the SME sector and size and scope of their transactions: .....	43
II.4 Financial intermediation .....	45
II.4.1 Banks: .....	46
II.4.2 Offering liquidity and payment services: .....	47

II.4.3	Transforming assets: .....	48
II.4.4	Information processing and monitoring borrowers:.....	50
II.4.5	Managing risks: .....	52
II.5	How banks overcome challenges when lending to SMEs: .....	53
II.6	Relationship banking: .....	56
II.6.1	More details about relationship-banking in the context of SMEs:.....	58
II.6.2	Soft information: .....	61
II.7	Benefits of relationship banking: .....	64
	Conclusion.....	71
III.	Methodology .....	72
	Introduction .....	72
III.1	Organic underpinnings of this study:.....	72
III.2	General case for the qualitative approach.....	75
III.3	Research method: Case study .....	82
III.4	Criticism of the case study method/approach: .....	85
III.5	The importance of the Context .....	90
III.6	Case study components.....	92
III.6.1	Selection of the case “banks”:.....	94
III.6.2	Selections of interviewees from within each bank:.....	98
III.7	Development of the interview themes and questions .....	108
III.7.1	Mapping the interview questions with the thesis research questions..	110
III.7.2	Techniques to Improve quality of interviews: .....	113
III.7.3	Ethical approval: .....	115
III.7.4	Pilot interviews .....	116
III.7.5	Interview protocol: .....	118
III.8	Thematic analysis .....	121
III.8.1	The first step.....	125
III.8.2	The second step .....	126
III.8.3	The third step.....	136
III.8.4	The fourth step .....	141



III.8.5	The fifth step .....	143
III.8.6	The sixth and final step .....	143
	Conclusion.....	144
IV.	Empirical context of the study: banks & SMEs in New Zealand .....	145
	Introduction: .....	145
IV.1	Banking in New Zealand: .....	145
IV.1.1	A historical overview of the New Zealand financial/banking system.	145
IV.1.2	Recent developments of the banking system .....	149
IV.1.3	Focal Banks & relationship banking .....	156
IV.2	SMEs in New Zealand .....	164
IV.2.1	Importance of SMEs in New Zealand .....	165
IV.2.2	SMEs numbers in New Zealand are no different from other OECD countries. ....	169
IV.2.3	Importance of bank finance to SMEs.....	172
IV.2.4	Small business-bank relationships: .....	174
	Conclusion.....	176
V.	Analysis & Discussion -I- .....	177
	Introduction: .....	177
V.1	Banking segments: .....	178
V.2	Small business definition: .....	181
V.2.1	Sector of activity: .....	183
V.2.2	<i>Complexity of the business:</i> .....	184
V.2.3	<i>Ethnicity of the small business owner/manager</i> .....	185
V.2.4	<i>Primary source of income:</i> .....	185
V.2.5	<i>Turnover:</i> .....	186
V.2.6	<i>Business lending:</i> .....	186
V.3	Taxonomy of the business banking relationship management model .....	187
V.3.1	Online management model: .....	189
V.3.2	Small business relationship model: .....	190
V.3.3	Medium sized business relationship model: .....	193

V.4	The lending approach and criteria used by banks to assess SMEs' loan applications: .....	201
V.4.1	The lending criteria .....	205
V.4.2	Possible outcomes from processing SMEs loan applications: .....	214
V.4.3	The non-segregation of loan underwriting to SMEs: .....	217
V.5	What is relationship banking to the five major bank brands in New Zealand? .....	224
	Conclusion.....	233
VI.	Analysis and discussion –II–: Advantages of the relationship banking model	235
	Introduction .....	235
VI.1	Cross-selling: .....	236
VI.1.1	Enhancement of assessment accuracy with every product sold.....	241
VI.2	Retention .....	243
VI.3	Referrals:.....	246
VI.4	As a strategy to assess a new industry and gain access to and a foothold in a niche market judged to be lucrative: .....	249
VI.5	Building trust, rapport, and the information transfer process .....	251
VI.6	To humanise the bank .....	256
VI.7	Understand SME owner/managers' motivations for being in business and understanding the story behind the numbers.....	258
VI.8	Enhanced understanding and evaluation of the overall context around the SME & its owner manager:.....	262
VI.9	Access to and assessment of Intangibles: .....	264
VI.10	To understand, assess, and mitigate risk around/related to the SME owner/manager:.....	268
VI.11	Developing the soft-data benchmark system: .....	272
VI.12	Information reusability: .....	276

VI.13	Reduction in the marginal cost of information production and spreading the fixed costs of products: .....	279
	Conclusion.....	281
VII.	Conclusion .....	286
VII.1	What does relationship-banking mean to the five major bank brands in New Zealand?.....	286
VII.2	How does relationship banking actually work? .....	289
VII.3	What are the sources of value (i.e. benefits) of relationship banking to the five major bank brands when dealing with SMEs in New Zealand and how do these banks secure these benefits?.....	290
	End note: .....	294
VIII.	References .....	295
IX.	Appendices .....	308
IX.1	Appendix 1: Consent Form for Participants .....	308
IX.2	Appendix 2: The participant Information Sheet .....	310
IX.3	Appendix 3: Interview schedule .....	312

## List of figures

Figure 1: Expected Return for the Bank as a Function of the Interest Rate Charged.	38
Figure 2: Asymmetry of Information and Credit Rationing. ....	39
Figure 3: A streamlined process of thematic analysis using Saldaña's 2009 model .	140
Figure 4: an early stage thematic map showing some themes, categories, & codes.	142
Figure 5: New Zealand break-down of financial system assets (2004) .....	150
Figure 6: Size of banking sector: selected countries .....	151
Figure 7: Stock market capitalisation: selected countries .....	151
Figure 8: Increase in registered bank and non-bank business lending.....	152
Figure 9: Genealogy of New Zealand banks.....	154
Figure 10: Increasing number of bank employees per branch .....	160
Figure 11: Number of SMEs per relationship manager .....	161
Figure 12: Relationship between number of SMEs and number of relationship bankers per region .....	163
Figure 13: Percentage of Enterprises by Employee Size Group and ANZSIC (February 2010).....	167
Figure 14: Average Real Profit per RME by Employee Size Group (March 2009) .	168
Figure 15: Current debt by source, last financial year at August 2004.....	173
Figure 16: Debt finance requested and received by source.....	173
Figure 17: years with main financial institution by business size.....	175
Figure 18: Segmentation of the banking activities by the 5 major banks .....	181
Figure 19: taxonomy of relationship banking within SME banking.....	196
Figure 20: stepwise function representation of the different segments of relationship banking.....	199
Figure 21: Cross-selling and the enhancement of assessment accuracy .....	242
Figure 22: Risk level as a decreasing function of character reputation .....	266

## List of tables

Table 1: Lending technologies .....	56
Table 2: benefits of relationship banking accruing to banks.....	65
Table 3: the case study, its subject, and object .....	94
Table 4: Interviewees attributes .....	107
Table 5: Mapping of interview questions with interview themes and the thesis's aim and research questions.....	112
Table 6: Phases of thematic analysis.....	125
Table 7: An example of data extract with two initial codes.....	128
Table 8: an example of a process in action .....	135
Table 9: Registered banks in New Zealand as of 28 February 2012 .....	155
Table10 : Comparative size and performance measures of the focal banks .....	157
Table 11: Number of SME units with 0-19 employees per region & number of corresponding business managers .....	162
Table 12: Number, Percentage, and Cumulative Percentage of Enterprises by Size (February 2010).....	165
Table 13: SME employment in New Zealand during the last decade.....	166
Table 14: Proportion of firms with fewer than 20 employees, New Zealand & OECD firm project data .....	171
Table 15: Criteria used in defining small businesses. ....	182
Table 16: A contrast between the HDBS and the SDBS .....	274

## **I. Introduction**

### **I.1 Background to the research:**

Business-bank relationships have been the focus of a considerable amount of research, certainly going back to the early 1960s (Hodgman, 1961) and potentially even earlier (Ongena & Smith, 2000). A significant body of literature exists discussing theoretical considerations relating to the relationships between financial intermediaries, especially banks and their business clients (Fama, 1985; Hodgman, 1961; Leland & Pyle, 1977; Ramakrishnan & Thakor, 1985). Over time, Small business (SME) finance has developed as a special area of interest and research into bank – small business relationship, and this area continues to develop (Baas & Schrooten, 2006; Berger & Udell, 2002).

Relationship banking is an exercise between two partners: a bank and its business client. For a better understanding of this relationship, and that of banks' contribution to economic performance, we are to study this relationship from both sides. Earlier empirical investigations into the benefits of relationship banking have largely looked at this model from the firm's perspective. Studies such as (Billett, Flannery, & Garfinkel, 1995; Hoshi, Kashyap, & Scharfstein, 1990; Lummer & McConnell,

1989; Slovin, Sushka, & Poloncheck, 1993) have focused on relationship banking benefits accruing to big companies while others like (Cole, 1998-USA; Peltoniemi, 2007-Finland; Perry, Cardow, Massey, & Tweed, 2006-New Zealand; Petersen & Rajan, 1994; Scott, 2006-USA; Uchida, Udell, & Watanabe, 2006-Japan) have focussed on the relationship advantages to the small and medium enterprises. A wide range of variables/aspects are covered in these studies, including the effect of the duration of the relationship, the number of bank relationships, the intensity of the relationship on the availability of loans with emphasis on the collateral requirements, and the interest rate charged.

## **I.2 Gap identification and motivation for the study**

While there is much research on relationship banking benefits accruing to businesses in general, and small businesses in particular, only very recently have a few empirical studies started investigating relationship banking benefits accruing to banks, such as (Bharath, Dahiya, Saunders, & Srinivasan, 2007; Ergungor, 2005; Puri, Rocholl, & Steffen, 2011). Like the current study, these studies were motivated by Boot's (2000) call to empirically investigate relationship banking benefits accruing to banks which was identified as a gap in the literature through his review paper on relationship banking. Boot (2000) stated, "The modern literature

on financial intermediaries has primarily focused on the role of banks as relationship lenders... (However) existing empirical work is virtually silent on identifying the precise sources of value in relationship banking. For example, while it is very plausible that banks acquire valuable information through relationships, and the empirical evidence is generally supportive of this, little is known about *how* banks obtain information, what type of information they acquire, and how they use this information” (p. 21) (emphasis in original).

Essentially, Boot identified that both benefits to banks constituted a gap in the literature, and also that this gap consisted of not only the benefits to banks but also what can be called the process of securing these benefits. Subsequently, the author of this thesis realised that Boot’s identified and highlighted research gap has not been fully addressed and the opportunity for a contribution existed in not just what the benefits were *but how* banks operationalized them. To delineate some further aspects of the gap raised by this realisation, the widely reported benefit of relationship banking, known as cross selling (Deakins & Hussain, 1994; Degryse & Cayseele, 2000), will be used as an illustration. To comprehensively address Boot’s question about identifying the precise source of value –in this case cross selling- it is not enough to establish an



association between cross-selling and relationship banking and the degree of that association. The answer should also be concerned with answering the following three questions for each benefit identified:

- 1- What type of information would allow banks to secure the cross selling benefit (as a source of value) from and through the use of relationship banking?
- 2- How do banks obtain that information? I.e. what process(es) do banks use?
- 3- How do banks use the information obtained to secure the cross selling benefit and maximise that benefit for the benefit of those banks?

Earlier studies relevant to this one established some very specific benefits by way of investigating the presence (or otherwise) of those benefits, and the degree of their presence. At no point in time did any of these studies make the claim that they were investigating how these benefits worked and how they were secured by banks. For example, (Bharath et al., 2007) clearly stated that the focus of their paper was to be “on establishing the existence and the nature of the benefits of relationship banking from the perspective of the lender”. That is by examining “whether establishing a

lending relationship translates into a higher probability of winning future lending as well as non-lending business for a lender” (Bharath et al., p. 370) i.e. testing for an association between existence of relationship banking and cross selling in the form of winning future lending and selling other non-lending banks’ products and services to the relationship managed clients. Also Ergungor (2005) study empirically examined the question of “the extent to which relationship banking adds value to the banks providing the service. That is, how profitable is relationship lending?” (Ergungor, 2005, p. 486). This study focused on the context of community banks with relationship banking-managed small businesses in the USA.

### **I.3 Research problem, propositions, uniqueness and importance of the study:**

#### **I.3.1 Research problem:**

To investigate the sources of benefits from relationship banking accrued by the five major bank brands in New Zealand when dealing with their small business customers and the processes/mechanisms for securing these benefits.

### I.3.2 Research questions:

Four research questions are considered:

1. What does relationship-banking mean to the five major bank brands in New Zealand?
2. How does the relationship-banking process actually work?
3. What are the sources of value (i.e. benefits) of relationship banking to these five major bank brands when dealing with relationship-managed small businesses in New Zealand?
4. How do these banks secure these benefits?

### I.3.3 Uniqueness of the study:

This study differs from previous studies in both substance and form in at least four main ways. First, it seeks to empirically identify the sources of value creation and value addition to the five main bank brands in New Zealand using the relationship-banking model to manage their SME clients from the banks business managers' perspectives.

Second, the emphasis is on processes involved in securing these benefits, for the benefit of banks, from the business manager's perspective.

Previous studies have only speculated about these processes from their statistical analysis.

Third, the study has unearthed and conceptualised new relationship banking benefits to banks. These benefits have also been analysed and how they are operationalised for the benefits of banks is documented here. These benefits haven't been raised by the banking literature before.

Finally, the research approach used is a qualitative approach, which has not been used by any of the previous studies made possible, thanks to the rare opportunity of securing and conducting interviews with 27 relationship bank managers in New Zealand from the five main bank brands. Consequently, the thesis also answers calls to for different methodologies in finance particularly those advancing qualitative approaches to finance (Bettner, Robinson, & McGoun, 1994; Burton, 2007; Frankfurter et al., 1994; McGoun, 2003). Among other things, this approach has facilitated the identification of the new benefits because it has allowed reporting straight 'from the horse's mouth' enabling a front-line report of the bank policy in action to be captured and analysed.

### **I.3.4 Contribution and importance of the study**

There are a number of important contributions this study makes. Starting with the specific contributions and moving to the more general, this section describes those contributions.

Banks can use a range of technologies to assess loan applications from their SME customers (Berger & Udell, 2006) (please see section II.5 below on lending technologies). For banks to choose the most appropriate technology, or technologies, to use, they have to make use of an economic appraisal methodology such as a cost-benefit analysis to assess the profitability and efficiency of each lending technology. Knowing the processes of how banks secure relationship banking benefits accruing to banks is very important, as those processes will certainly entail costs such as the employment of relationship managers, and those costs must be taken into account for a proper cost-benefit analysis and appraisal of the relationship banking technology. Additionally, securing those benefits requires knowledge of the level that these benefits occupy in the lending process, who is responsible, and when. To maximise these benefits to banks, all these points must be taken into account, training must be provided, and development of best practices to secure the maximum level of each benefit must be identified.

Knowing at what point in the process each benefit will happen would allow the bank to be ready to seize the benefit and to specify and (may be even) automatise the seizing of the benefits.

Furthermore, in order for a cost-benefit analysis to be effective, all the benefits plus costs must first be identified and accounted for in the cost-benefit analysis of each model including the relationship technology/model. While some relationship banking benefits have been identified in the extant theoretical studies, and some of these have been empirically tested, this study has identified further benefits not currently present in the literature; such as relationship banking as a humanising mechanism for the bank's dealings with its relationship managed SME clients. This thesis found trust in banking to be very important, but banks seem to be the least trusted business organisations (Edelman Trust Barometer, 2012; Ernst & Young, 2011) and were reported as being viewed as unfriendly. This creates a trust issue for banks. However, through the use of relationship banking with a relationship manager acting as the human face of the bank, and being the point of contact for dealing with the SME client on a one-to-one basis, banks are able to counter that view of untrustworthiness and unfriendliness.

Furthermore, this benefit is even more important in the current banking environment as the recent (and on-going) financial crisis has raised the

profile of banks in the wider society. People, including SME owner/managers, are thinking about banks and their role in their lives. Banks have become a locus of much derision and mistrust due to the mortgage crises in the western world - particularly the USA and UK and, more recently, elsewhere. People are thinking about banks more and how their banks and their relationships with banks affect them and their lives. As people now dislike banks and feel they can't trust them, it is important for banks to be seen as 'human' and also as 'good corporate citizens'. Relationship banking is a way for banks to pursue this 'brand personality' in the wider market and counteract the effects of the bad publicity generated by the financial crisis.

For a proper appraisal of relationship banking technology these newly identified benefits need to be accounted for. So, in a further contribution, this study also identifies brand new benefits, the process of their identification and how banks secure them in the bank-SME relationship.

The thesis has also succeeded in classifying relationship banking benefits, both the old and the newly identified, into taxonomies of benefits, such as the risk-return taxonomy. This shows clearly how these taxonomies both can and do benefit banks, and how they help to define

and position relationship banking within/at the heart of the finance discipline when finance is defined as increasing return and lowering risk.

Empirical studies begin with a decision about definition. Decisions then follow regarding measurements and which proxies to use for measuring the different aspects of the focus at hand. In the case of relationship banking these are its costs, its length or depth. Therefore, the definition is pivotal. However, this study has shown how -from the bankers' perspectives- the oft-quoted definition of relationship banking is missing critical elements. A lengthy discussion of these missing elements follows in the analysis chapter. Future studies dealing with relationship banking, particularly empirical ones, have to consider this issue.

There is a large amount of literature detailing the benefits of relationship banking to small businesses and, as previously mentioned, significantly less looking at the benefits to banks. For these benefits to keep flowing to SMEs, Profit oriented banks<sup>1</sup> need to be convinced about the value of relationship banking. This study can contribute to banks' understanding of the value of the relationship to them through the outcomes of an analysis such as will be undertaken in this thesis, hence contributing to the likelihood of a continuation of this model of banking for SMEs.

---

<sup>1</sup> Although not for profit banks do exist in many countries such as New Zealand, this thesis is only concerned with profit oriented banks.



Acknowledging the paucity of research on how the bank-business relationship banking works in general, Berger and Udell (2002) stated that “Despite the recent academic focus on relationship lending, there is remarkably absent in the literature a fully satisfying analysis of precisely how bank-borrower relationships work” (p. F33).

This study will contribute towards that analysis of how the bank-SME relationship works because this analysis is prerequisite for addressing the thesis’s main aim, which is how banks secure relationship banking benefits.

Other authors have also raised the issue, though from a different perspective. An example of this is Udell (2008); “Because banks comprise an important pillar in the architecture of any financial system, it is critical that we understand what makes these financial intermediaries tick... In short, if we are to understand the contribution of commercial banks to economic performance, we must first understand how they lend money. This, in turn, requires an understanding of relationship lending and its role in SME loan underwriting” (p. 94).

Part of that understanding is understanding the benefits of relationship banking to banks and it is to this literature that this thesis seeks to make further contribution.

## **I.4 No human endeavour is perfect: scope and limitations of the study:**

The thesis focus is on investigating and gaining a deeper understanding of the sources of benefits from relationship banking accrued by the five major bank brands in New Zealand when dealing with their SME customers and the processes/mechanisms for securing these benefits. The primary data gathered and used is from the perspective of those working, or those who have worked, as bank relationship managers. The method used claims analytical generalisation and at no point in time seeks a statistical generalisation. Hence, generalisations of the thesis's findings to other contexts and with other banks must be done with caution and requires further investigation.

Furthermore, no attempt has been made to link the thesis findings to the banks' performance. However, a suggestion is made for future investigations, to test the link(s) between the thesis' findings and banks' performance.

## **I.5 Thesis organisation**

The structure of this thesis proceeds as follows. Chapter II, the framework, builds the context for this research leading to the delineation

of the research gap, the research problem and the research questions identified I.3.1 and I.3.2 above. The next chapter comprehensively elaborates on the methodology of the research used to address the research problem and answer the research questions. This is followed by a discussion on the empirical context of the study, New Zealand, which is the extension of the framework but more specific to the empirical context of the study. Here discussion is more focused on banking/banks, SMEs, and relationship banking. Chapters V and VI present analysis and discussion of the empirical results. Chapter VII concludes the thesis by summarising the main findings and implications of the research, including suggestions for future research in this area.

## **II. The framework of the study**

### **Introduction**

This chapter sets the scene for the whole thesis in that it builds the framework for investigating the thesis research aim and questions. It begins with some prior research on SMEs and banking in general in section 1. Section 2 reports on some issues and characteristics of SMEs, making the case for the specificity around SME finance. The next section is about challenges faced by banks when dealing with SMEs. Then, after positioning banks as a financial intermediary in section 4, section, 5, deals with how banks try to overcome those challenges when lending to SMEs. The emphasis is on relationship banking, which section 6 elaborates on. Finally, section 7 reviews some of the benefits accruing to banks from relationship banking.

### **II.1 Prior research about SMEs and banking:**

Some of the predominant themes in the literature concerned with small business (SME) banking focus on the importance of the availability of finance, factors influencing bank supply of finance, and the key factors influencing SMEs about bank choice. At the macro end of the spectrum, the debate focuses on whether there is a ‘finance gap’, which may inhibit

the growth of SMEs, leading to a less than desirable growth in the economy overall. At the micro end of the spectrum, topics include the pricing of banking services to SMEs and the transparency levels with which this pricing is easily comparable across banks by SMEs.

The finance gap is suggested as a perennial issue for SMEs and is generally defined as a shortage of finance from the supply side for SMEs to fund growth, expansion and other core activities. Keasy and Watson (1993), Niskanen & Niskanen (2010), and Storey (1994) suggested SMEs often experience difficulties raising new finance and/or are dissatisfied with the terms and conditions attached to bank finance. Informational asymmetry is often stated as the cause of this frustration for SMEs, as witnessed by a large body of research including Ang (1992) and Gregory, Rutherford, Oswald, and Gardiner (2005). Baas & Schrooten (2006) discussed the information asymmetry issue, i.e. the problem of SMEs having information internally but bankers not having access to it, and how this leads to a premium on interest rates.

The conventional wisdom that SMEs want to grow and cannot access capital has been criticised over recent years culminating in the “contentment” or “happiness” hypothesis by Vos, Yeh, Carter, and Tagg (2007). Vos et al. (2007) hold that “gap” studies are biased by a

“world view”, assuming that like listed companies, SMEs are wealth maximisers or growth seekers, justifying the approach of rational risk–return models. The contentment hypothesis, however, stems from a reality, specific to small and medium sized enterprises (SMEs); that money is a means to an end, not the end itself. Independence and control are often given reasons for the difference in SME financial behaviour (Curran, 1986; Jarvis, 2000) compared to what might be expected of a publicly listed firm (Vos et al., 2007, p. 21). Thus, SMEs choose not to participate in the external capital markets out of a feeling of contentment in being independent, in control of the business and in sustaining the business (Vos et al., 2007). This happiness hypothesis is supported by two sets of data from the United States and United Kingdom. Further, Shen (2007), using the New Zealand Business Benchmarking Survey<sup>2</sup>, confirmed the contentment hypothesis refuting the finance gap, a result that was arrived at by an earlier study of Austin, Fox, and Hamilton (1996) commissioned by the New Zealand Ministry of Commerce. The Austin et al. (1996) study concluded that it was the preference of SMEs’ managers/owners not to grow that hindered the growth of bank lending to SMEs (demand side) not the other way around.

---

<sup>2</sup> The annual survey produced by the Management Research Centre, Institute of Business Research at the University of Waikato.

Research shows there is a range of reasons why SMEs choose a particular bank, including prior personal banking experience, knowing someone in a bank, referral, locational proximity and cost of services. Mazur (2007) found that where the SME customer already has a personal account with the bank, chances are good that they will also open a SME account with that same bank. Binks, Ennew, and Mowlah (2006) find that some important factors of bank service include basic products and services that are offered, transactions charges for account services, interest rates, criteria for qualifying for a loan, knowledge and understanding, price and operations.

Lucey (1990) noted that many small firms want a bank that is conveniently located. A study of internet banking found that around 50% of SMEs want to have a branch five minutes away rather than have free online services and no local branch, according to Mackintosh (2001). A 2006 survey of SMEs in the UK found that although most banks are spending considerable money and time to promote their online service, SME owners believe that having their bank nearby is the most important bank characteristic for conducting their firm's banking business. 62% of SMEs used a local or regional bank as their primary bank, because they wanted to be physically close for cash deposits; this was especially the

case for retail enterprises (Scott & Dunkelberg, 2006). However, this might not apply in New Zealand, due to the well-developed electronic payment system. The majority of retail transactions are electronic point of sales (EFTPOS) which cover both credit (e.g. Visa and Mastercard) and debit cards. Credit card transactions are predominantly handled through EFTPOS with a personal identification number (PIN) rather than signature (Boulanouar & Locke, 2009).

Gill, Flaschner, and Shachar (2006) investigated the impact of “person-related” service characteristics (empathy, politeness and similarity) and “offer-related” service characteristics (customisation, competence and promptness). That examination of business clients’ trust with their current bank service representatives, based on the length of the relationships with their banks, indicated that all six factors were related to trust building in general. Nevertheless, there were factors that were more salient at different periods of the SMEs’ relationship with their banks, and customisation was found to be particularly important at crucial periods in the business life cycle.

Dorfman (2007) drew together the necessary success strategies for banks to acquire the loyalty of SME owners, suggesting four strategies:

- Use customer service as a strategic weapon.



- Create intimacy and trust by knowing your customer.
- Make banking easy, convenient and painless.
- Differentiate value for your most profitable customers.

According to Enrich (2007), one approach that banks used in the US to obtain new SME clients was to take more risk in initial lending decisions. Enrich suggested that banks were extending credit to start-ups with practically no track record, accepting lower-quality assets as collateral and imposing fewer restrictive covenants on borrowers to attract clients. Early studies by Greenbaum, Kanatas, and Venezia (1989) and Sharpe (1990) considered the conditions under which lenders subsidise borrowers in early periods and then how they are reimbursed in later periods.

Lucas and Davis (2005) suggest that banks are consolidating their lending operations in remote locations and are relying more on heuristics that promote arms-length relationships rather than on branch officers with access to vital private knowledge. They argue that SMEs often have unique circumstances and the strong ties developed between branch officers and these business owners provide access to critical private knowledge that is otherwise unavailable. On the other hand, Ergungor (2005) provides evidence supporting the view that competition reduces

the benefits of bank–borrower relationships, making relationship loans more risky and less profitable.

## **II.2 SME finance:**

SMEs have a need for capital, and typically their financial structure gives rise to very specific issues. Traditionally, these issues have been viewed as financial problems or constraints. Contrary to that view, one current proposition is that SME financial structures and characteristics are a reflection of managerial decisions and preferences (Gibson, 2001). This suggests that there are natural constraints on small firms, “given [for instance] the low asset base from which many commence and are prepared to operate within so as to maintain control of the business” (Holmes, Hutchinson, Gibson, Forsaith, & McMahon, 2003, p. 141). This view is echoed by recent studies such as those by Vos et al. (2007) discussed earlier and Reddy (2007). Reddy claims that for SMEs, the primary objective is not growth, but rather to provide for a family and that business owner-operators can be content with less.

Various determinants of the capital structure decision between equity and debt in small firms are noted in the literature (Coleman, 2008). These determinants range from the usual informational opacity to the high costs of raising public loans and equity underwriting.

When SME owner-managers need extra capital, they have an inclination and strong incentives for issuing external debt rather than seeking external equity from investors. This choice is explained by small firms' owner-manager not wanting to dilute ownership claims, and shunning any external participation in decision making about their firms that would lead to loss of control (Berger & Udell, 1998). External equity is thought to come with more control rights than covenants associated with debt instruments. This disposition is consistent with findings that independence and autonomy motivations are behind starting, owning and managing SMEs (Collins & Moore, 1970; O'Connor, 1983; Roberts & Wainer, 1971; Scheinberg & MacMillan, 1988; Stanworth & Curran, 1973; Storey, 1982). Ultimately, independence and control are the primary reasons behind the financial behaviour of small firms (Curran, 1986; Jarvis, 2000).

SMEs typically do not raise debt or equity directly from the public. An inability to access such funds is due to the nature of these public markets. Public loans and equity underwriting involve several significant costs - including underwriting and administrative expenses - which small firms find prohibitive. The former consist of the underwriting and selling fees paid to the underwriter. The latter comprise legal fees, audit services and

printing costs. Berger and Udell observed that “many of these costs are essentially fixed and create economies of scale in issue size. Given that issue size and asset size of the firm are strongly positively related, these economies of scale in issue size maybe difficult for small and mid-sized businesses to overcome” (1998, p. 628). Financial intermediation services are, therefore, essential for most SMEs.

The supporting systems that are normally used to offer feedback and to support decision making concerning the management of finances, assets and liabilities are also found to have an effect on SMEs. Financial management and accounting systems according to McMahon and Holmes (1989) are essential components. However, SMEs do not invest in in-house systems with internal specialists to operate them. These investments cannot be justified given SMEs’ level of business activity. SMEs do not adopt and do not use these sophisticated financial management systems (Holmes et al., 2003). SMEs have few employees, and according to Ang (1991), typically lack the necessary expertise to provide detailed financial statements. Additionally, SMEs are not legally required to have audited financial statements, nor do they have any legal requirements to provide International Financial Reporting Standards (IFRS) compatible financial statements for shareholders (Ernst & Young,

2009). The lack of external requirements for detailed financial statements coupled with internal constraints may result in less than sophisticated financial management.

Finally, SMEs have other distinguishing features, particularly firms in commencement phase that are not yet established in the market. One feature is the absence of business assets (Mann, 1998) that external capital providers such as banks can assess and accept as collateral. Other features include a lack of audited financial statements (Berger & Udell, 1998), a limited financial history of payments (Avery, Bostic, & Samolyk, 1998), and limited profitability that external capital providers can use in assessing the credit worthiness of SME borrowers.

### **II.2.1 Information asymmetry and SME finance**

Information asymmetry poses a significant problem for banks dealing with businesses and the problem is argued to be more pronounced when a smaller business is involved. The issue relates to the difference in terms of the information available to the bank and that which is known to the business.

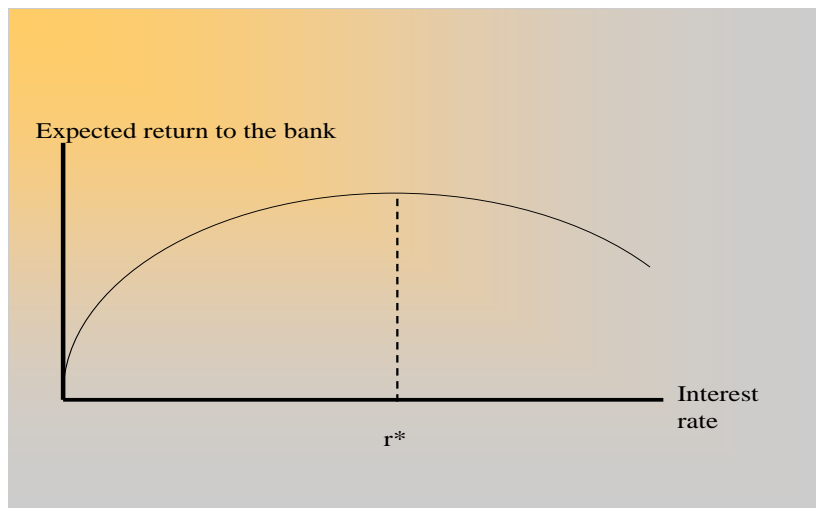
Information asymmetry was raised as an issue in a study of financial markets by the 2001 Economics Nobel Laureate, Joseph Stiglitz in a seminal work with Andrew Weiss (Stiglitz & Weiss, 1981) pointing to

the problem of adverse selection and credit rationing arising from information asymmetry.

They stress that in such cases interest rates lose their resource allocation function. The suggestion is that when a financial institution raises interest rates due to being unable to distinguish between borrowers at differing levels of risk, borrowers with the riskiest investment projects are exactly those who are willing to pay the highest interest rates. They are willing to pay this high price because they perceive their probability of repaying the loan to be low. If a borrower took on a high-risk investment and succeeded, the borrower would become extremely rich. However, a lender wouldn't want to make such a loan precisely because the investment risk is high; the likely outcome is that the borrower will not succeed and the lender will not be paid back. Thus, increasing interest rates could increase the riskiness of the bank's loan portfolio, either by discouraging safer investors; or by inducing borrowers to invest in riskier projects and therefore, the banks profit could be decreased. Lenders do not, therefore, raise interest rates even when there is too much demand for the market to meet. This is because the expected return by the bank may increase less rapidly than the interest rate, and, beyond a point, may actually decrease, as depicted in Figure 1 below. The supply curve thus

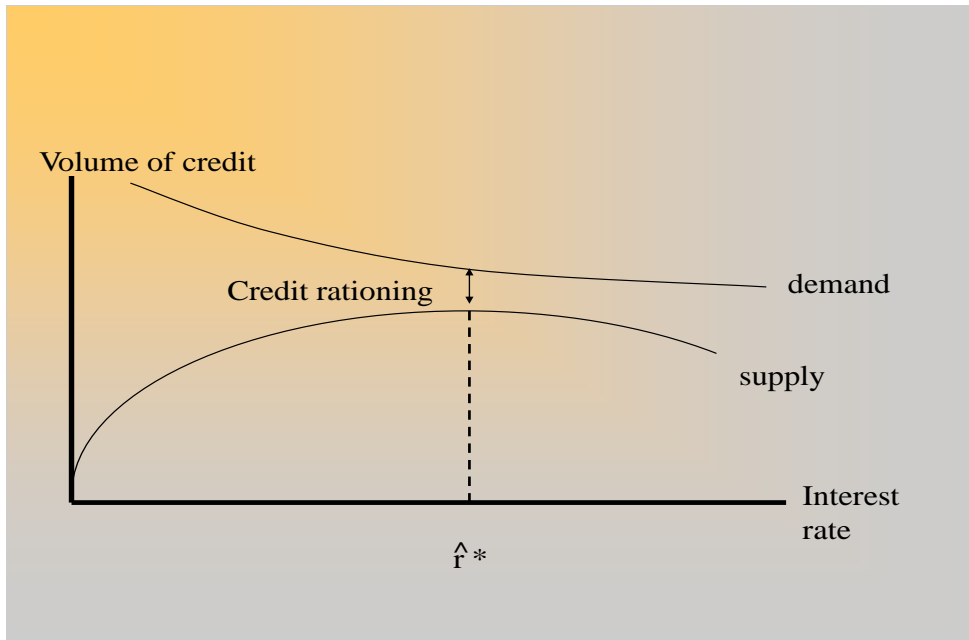
slopes towards the right and may in some cases, not intersect with the demand curve at all (Figure 2 below). In such cases, the supply and demand for funds do not balance. Therefore, borrowers find themselves unable to procure the capital that they believe they require, and credit rationing occurs (Stiglitz & Weiss, 1981).

Figure 1: Expected Return for the Bank as a Function of the Interest Rate Charged.



Source: Freixas and Rochet (1997).

Figure 2: Asymmetry of Information and Credit Rationing.



Source: Freixas and Rochet (1997).

Given that asymmetric information problems tend to be much more acute in small firms than in large firms, it is not surprising that small firms suffer more from credit rationing. This is because with small businesses outside stakeholders face several information problems. Some of these problems are discussed in the next section.

### II.3 Challenges and issues for banks when dealing with SMEs:

It is well documented that when interacting with SMEs seeking funds and other financial services, banks are confronted with a number of challenges that are typical to this category of business (Ang, 1991; Berger & Udell, 2003; Holmes et al., 2003). In particular, the lack of



readily available quality information in the public domain about individual SMEs raises costs. Also, most SMEs have no statutory obligation to file audited financial statements. These challenges and some of the others discussed in this section tend to be inversely proportional to the size of businesses that banks deal with. In this section, three challenges will be discussed; opacity, information asymmetry, and size issues.

### **II.3.1 Opacity:**

Opacity is related to the ability of a SME to communicate clearly pertinent information to outside stakeholders including the capital market (Berger & Udell, 1998). Furthermore, Berger and Udell (1998) describe this issue of information opacity as the hallmark of SME finance. The causes of this opacity are numerous (Holmes et al., 2003). One is the private nature of contracts between SMEs and their different stakeholders such as employees, suppliers and customers. These contracts are neither publicly visible nor widely reported in public media, which makes learning about SMEs from their contracts with other parties almost impossible. This is in contrast with contractual arrangements entered into by listed companies, which are widely reported in the media or at least in some specific media and can be accessed by the public.

Another source of opacity is the quality of data generated by the SME for review by outside stakeholders such as finance providers. This may be due to the age of the business; if it is in an early stage in its growth cycle there will not be many records showing financial history or profitability. SME people may not have the managerial talent and resources to come up with data useful to the stakeholders (Ang, 1991).

Because SMEs are not legally required to prepare International Financial Reporting Standards compatible financial statements, the absence of audited statements is another contributing factor. Financial statements are tools used by businesses to account for the use of funds and their operating activities. The aim of financial accounting in general and of financial statements in particular is to provide valuable information to outside users to learn about the financial aspects of the firm and help them to make sound and efficient economic decisions. However, the absence of financial reports suggests that SMEs are opaque at least in comparison with businesses that do promulgate financial reports.

SMEs that are keen on signalling good performance to banks do take action. Signalling might take the form of joining a local chamber of commerce, using a reputable accountancy firm, and/or joining a mentoring program. However, often banks experience difficulties in

drawing inferences as to the quality of the signals emanating from small firms (Ang, 1991). At the heart of this problem are the differences in expectations between SMEs owners/managers and banks. Usually, entrepreneurs are found to be more optimistic about their ventures than outside stakeholders. The SME owners/managers are, however, aware of this discounting and the outside stakeholders know that the owners/managers expect a reduction of their own optimism (Ang, 1991). This situation leads to a tension between the two parties which represents another facet of the opacity issue faced by banks when interacting with SMEs.

### **II.3.2 Information Asymmetry**

Information asymmetry poses a significant problem for banks dealing with SMEs. The issue relates to the different levels of information available about the SME and/or its owner manager that is known to the bank and that which is known to the business owner manager. For example, the following story about Apple illustrates the issue of moral hazard which is the second by-product of information asymmetry after adverse selection, as referred to in section II.4.4 below. Apple, then a small firm, borrowed money with a pre-arranged agreement to use for product development. However, and reflecting typical post-contract

opportunism, the Apple decision makers spent the funds on marketing activities. Luckily for both lender and firm, it worked. However, the lender gained nothing extra from the engagement of the Apple company into the extra risky activity and it could have been detrimental to the repayment of the loan (Borrmann & Tripe, 2008).

### **II.3.3 Size of the SME sector and size and scope of their transactions:**

The SME sector is characterised by two criteria, first the very large number of entities (Ministry of Economic Development, 2005), and secondly the lack of homogeneity among those entities from the sector. These two criteria make the risk of each SME different, which in turn makes it extremely hard for banks to evaluate small firms' financial risk (Borrmann & Tripe, 2008). Banks have to evaluate each and every business separately, and this issue of risk assessment is exacerbated by two more factors related to the size and scope of SMEs transactions (Ang, 1991).

One factor is the high fixed costs that banks have to pay to gather information about a transaction conducted by a typical SME. Most bank transactions incur a fixed cost component which doesn't vary with the transaction size. Furthermore, this type of transaction tends to be very

small both in scope and scale whereas some of the costs incurred are fixed. For example, when a bank collects a piece of information that it considers to be important in order to process a very small loan application from one of its SME customers, it nevertheless incurs a fixed cost that would be the same if the loan application was for a significantly larger loan.

The other factor concerns incentives for a third party to collect information on behalf of the bank, and then sells it to the bank (Ang, 1991). This third party could be an outside analyst or a rating agency. When the cost of collection that the third party has to pay is compared with the sale price of the information in question, as well as the very small size of the market for this type of information, the involvement and the investment by that third party may not be fully justified. However, there is some evidence that this view about the third party might not be entirely accurate. In Australia and New Zealand, for example, most banks would seek information about their potential SME borrowers and their owners/managers from VedaAdvantage<sup>3</sup>, the debt collection agency, to check their credit history. This suggests that a third party agency that does some kind of creditworthiness monitoring of small firms and their

---

<sup>3</sup> Formerly known as Baycorp, it is the largest credit bureau in Australia and New Zealand. It provides credit reports about businesses and individuals (<http://www.vedaadvantage.com/>).

owners/managers, indeed, exists, even if it does not collect financial information about them.

While many of those risks can be reduced by the use of different lending tools, such as collateral and technologies or practices like relationship lending, nonetheless, the risk of default increases the costs of lending to SMEs (Borrmann & Tripe, 2008).

Before talking about how banks as the primary source of external funding for SMEs (Ministry of Economic Development, 2010), the next section will provide a context for banks as a financial intermediary, followed by how banks try to overcome these challenges to assess risks, and price loans when lending to SMEs.

## **II.4 Financial intermediation**

Financial intermediation is the process by which fund providers deposit their capital surplus with financial intermediaries, who in turn lend to capital users. In essence, they mediate between the providers of funds and the users of these funds. According to Freixas and Rochet (2008), Greenbaum and Thakor (2007), and Matthews and Thompson (2008), these financial intermediaries predominantly fall into one or two categories. One group comprises those who directly accept deposits from depositors and make loans to borrowers. Examples of these are banks and

credit unions. A second group is made up of those who purchase securities and hence indirectly provide capital by means of the capital market rather than directly making loans as banks do. Insurance companies and pensions funds are two examples of this category.

#### **II.4.1 Banks:**

Banks are a specific form of financial intermediary and are commonly characterised as "an institution whose current operations consist in granting loans and receiving deposits from the public" (Freixas & Rochet, 2008, p. 1). The intermediation process from the banks' perspective focuses on asset and liability management. A core activity of a bank is receiving liquid and convertible (on demand) deposits and transforming these into medium and/or long term loans. The extraction of a return from such activity is associated with risk, default risk and withdrawal risk in particular (Matthews & Thompson, 2008).

Banks play a pivotal role in the allocation of capital in the economy (Merton, 1995). Specifically, four main functions characterise the value creating services of banks in the intermediation arena (Casu, Girardone, & Molyneux, 2006; Freixas & Rochet, 2008; Heffernan, 2005; Matthews & Thompson, 2008). These functions are detailed next.

### **II.4.2 Offering liquidity and payment services:**

For banks, the main source of funding, as alluded to previously, comes from their customers' deposits. However, these customers, faced with the lack of knowledge about future events, often have a preference for liquidity and want to be able to withdraw their deposited funds on demand. Banks are able to provide these deposit and liquidity services (Diamond & Dybvig, 1983), offering a broad range of accounts, such as cheque accounts, and other on call facilities.

Facilities to make payments is another service that banks provide for their customers; usually defined as “any organised arrangement for transferring value between [their] participants” (Casu et al., 2006, p. 25). Throughout history, people, in their normal course of life, have traded with each other, exchanging what they have extra for what they need and/or want. At first, the barter system was used as a clearing system. Over time, that system proved to be inadequate due in many cases to transportation, storage and costs. Money was an excellent discovery that changed forever the transfer of ownership claims between trading parties. Also, the concept of money has broadened so much that banks are able to facilitate the transfer of funds between traders, enabling them to make payments using a variety of payment services. These include writing



cheques from one's current accounts, electronic-based types of transaction such as the use of credit and/or debit cards, and more recently, web-based types of payments completed over the internet. Furthermore, with recent technological progress, banks have been able to offer easy access and relatively cheap web- and mobile phone-based facilities.

### **II.4.3 Transforming assets:**

The second function performed by banks is that of qualitative asset transformation (Greenbaum & Thakor, 2007). Lenders and borrowers have different preferences and requirements. For example, lenders often want to be able to access their deposited funds whenever they want. Conversely, borrowers want to retain their borrowed funds over the life of the project or investment. Banks transform the nature of claims or the asset attributes when they act as intermediaries between those lenders and borrowers in order to accommodate their<sup>4</sup> ideals (Gurley & Shaw, 1960). According to Matthews and Thompson (2008), this function comprises size transformation, maturity transformation and risk transformation.

---

<sup>4</sup> i.e. lenders and borrowers

Often lenders have small amounts of surplus capital whereas borrowers are in need of bigger amounts of funds for their projects. Banks perform size transformation by collecting smaller amounts of capital surplus from depositors, bundling them together into bigger parcels and then lending them to borrowers.

The next transformation function is that of maturity. Capital surplus units want to be able to access their funds whenever they want and/or need them, whereas capital users in deficit want security of funds over the life of the project or investment. Banks act between the two units via transforming securities - with short maturities from the former, into securities with longer maturities to the latter.

The third and final transformation is risk. Lenders prefer assets with a low risk and want their money to be safe. In contrast, borrowers use borrowed funds to engage in operations that carry a risk of default and might result in them not being able to pay back the funds they borrowed. Also, borrowers are predisposed to pay a higher price than that necessary to reward lenders where risk is lower. As financial intermediaries, banks are capable of altering and minimising risk using a number of tools and techniques, such as investment diversification, loans pooling, and the

screening and monitoring of borrowers. Some of these, specifically in dealing with their SME clients, will be elaborated on in section II.4.5.

#### **II.4.4 Information processing and monitoring**

##### **borrowers:**

This third function relates to banks performing one of their core activities as a financial intermediary, namely granting loans to capital users in deficit, and thereby having to manage the problems and difficulties arising from imperfect information concerning borrowers. This asymmetric information issue which Casu et al. (2006, p. 484) described as “the imperfect distribution of information among parties to a contract” arises regularly. An example is where a borrower is likely to have more information about the project for which a loan is sought than the bank has. Information asymmetry can give rise to situations of adverse selection and moral hazard.

Adverse selection occurs from pre-contractual opportunism where the bank is unable to distinguish between the qualities of the different projects presented for funding by the different borrowers. However, these borrowers know more about the projects, and as a result of this problem, the bank might end up selecting the bad projects (Matthews & Thompson, 2008).

Moral hazard occurs from post-contractual opportunism whenever a contract between two or more parties creates incentives for one party to act against the interests of the other party (Heffernan, 2005). For example, a SME borrower may act in a way that is detrimental to the repayment of the loan by engaging in more risky activities than that initially agreed with the bank.

To minimise default and other risks associated with lending, banks will seek to reduce information asymmetries with their associated pre- and post- contractual problems by processing information from and about borrowers. Various technologies provide opportunities in this regard. First, borrowers and their loan applications may be screened to reduce the likelihood of funding the bad projects and/or bad borrowers mitigating the adverse selection problem. This can be done, for example, by seeking out relevant information to examine borrowers' credit worthiness. Secondly, in dealing with the moral hazard problem, banks monitor borrowers and their behaviours by collecting information and ensuring that the borrowers adhere to the terms of their contracts as well as refraining from acting in a manner contrary to the bank's interests.

### **II.4.5 Managing risks:**

Banks, as financial intermediaries, face several interdependent risks, some of which are inherent, such as liquidity or funding risks and credit or default risks, due to the nature of banking activities that involve taking deposits and extending loans. Profit oriented banks will assume risks and work to manage them to avoid losses. The management of risk is the third major activity for banks. Various taxonomies of risk have been proposed and these typically include credit, liquidity, and interest rate risks. These are briefly discussed in turn.

Credit risk, also called default risk, is described in the Basel I Accord as “the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms” (Basel Committee on Banking Supervision, 2000, p. 5). Banks manage this type of risk using different techniques. The requirement for collateral from borrowers is typical. Heffernan (2005) sees default risk as associated mostly with moral hazard and information problems, suggesting that “banks must monitor their borrowers to increase their return” (Heffernan, 2005, p. 105) and minimise the probability of default on a loan agreement.

Liquidity or funding risk arises from banks providing liquidity-related services to depositors. This risk occurs when a bank is obliged to make

unexpected payments when depositors exercise a withdrawal from an on-call account. Banks have a range of tools and facilities to reduce their exposure to liquidity risk, such as increasing their holdings of near cash and readily marketable assets like treasury bills and or funding long-term loans with equally long term deposits.

Interest rate risk arises from the maturity transformation activity performed by banks. When banks fund long-term loans using short-term deposits, for example, costs of funds may rise above the income generated from interest received.

Overall, a profit oriented bank will aim to maximise returns on earning assets and minimise the risk of default.

## **II.5 How banks overcome challenges when lending to**

### **SMEs:**

Information is important to banks. When lending to SMEs, financial intermediary institutions in general and banks in particular have developed a range of tools and techniques, such as debt covenants and relationship lending, to gain information, overcome the challenges detailed in section II.3 above, and to aid decision making regarding issues like risk assessment and loan pricing. These tools and techniques have been further facilitated by technological progress. Berger and Udell

(2006) provided a taxonomy to organise and classify these tools and techniques, which they have called ‘lending technologies’. They describe a lending technology “as a unique combination of primary information source, screening and underwriting policies/procedures, loan contract structure, and monitoring strategies/mechanisms” (Berger & Udell, 2006, p. 2946). The primary objective of these technologies is to minimise costs, including the risk of poor decisions, and to increase banks’ returns. This taxonomy of lending technologies seems to have gained wide acceptance among specialists in the finance literature (Ayyagari, Demirgüç-Kunt, & Maksimovic, 2010; De Haas, Ferreira, & Taci, 2010). These technologies can be divided into two categories by the type of borrowers -opaque and/or transparent- or the source of primary information used - soft and/or hard:

1. Transactions lending technologies, including financial statement lending, SME credit scoring, asset based lending, factoring, fixed-asset lending, leasing, and
2. Relationship lending technologies in which “the financial institution relies primarily on soft information gathered through contact over time with the SME, its owner and the local

community to address the opacity problem” (Berger & Udell, 2006, p.2951).

Each technology can be used in combination with another technology or other technologies. This suggests that one technology can be used as a primary method of information source, which can then be supported by other technology(ies), and that these technologies are not interchangeable. Furthermore, “In some cases, the technologies may be most efficiently deployed in a particular organisational form or unit that is dedicated to that technology. The unit may be an entire financial institution (e.g., a leasing company offering only business leases), or a separate department, division, or subsidiary (e.g., an asset-based lending department of a commercial bank or finance company)”(Berger & Udell, 2006, p.2948).

Some of these details about lending technologies are summarised in Table 1 (below).



**Table 1: Lending technologies**

<b>Technology</b>	<b>Type</b>	<b>Borrower</b>	<b>Information</b>
Relationship lending	Relationship	Opaque	Soft
Financial statement lending	Transaction	Transparent	Hard
Asset-based lending	Transaction	Opaque	Hard
Factoring	Transaction	Opaque	Hard
Leasing	Transaction	Opaque & Transparent	Hard
SME credit scoring	Transaction	Opaque	Hard
Equipment lending	Transaction	Opaque & Transparent	Hard
Real estate-based lending	Transaction	Opaque & Transparent	Hard
Trade credit	Transaction	Opaque & Transparent	Soft & hard

Source: Taketa and Udell (2007)

Finally, while the current research uses this taxonomy of lending technologies as a framework of reference to build and present its case, it will later be argued and suggested in the analysis section that this taxonomy might not apply per se to the relationship model. The next section defines relationship banking as presented in the finance literature.

## **II.6 Relationship banking:**

Although Boot (2000) asserted that there was no precise definition of relationship banking, by 2011 a generally accepted definition had been

developed. An early definition was provided by Ongena and Smith (2000), who stated that it is “the connection between a bank and a customer that goes beyond the execution of simple, anonymous, financial transactions” (p. 4). However, they went on to add two dimensions to this definition; time or the duration of this connection, and scope, being “the breadth of services offered by the bank to its customer” (p. 5).

A more elaborate and widely used definition is that of Boot (2000) who notes that relationship banking is “the provision of financial services by a financial intermediary that:

- i. Invests in obtaining customer-specific information, often proprietary in nature; and
- ii. Evaluates the profitability of these investments through multiple interactions with the same customer over time and/or across products” (p. 10).

Then, influenced by Berger (1999), Boot added three conditions for relationship banking to be accorded as present:

- i. “The intermediary gathers information beyond readily available public information [through screening loan applications and monitoring] ;

- ii. Information gathering takes place over time through multiple interactions with the borrower, often through the provision of multiple financial services;
- iii. The information remains confidential (proprietary)” (Boot, 2000, p. 10).

### **II.6.1 More details about relationship-banking in the context of SMEs:**

At this stage, it must be stated that Berger and Udell wrote a series of papers on SME finance, such as (Berger, 1999; Berger, Klapper, & Udell, 2001; 1995, 1998, 2002, 2003, 2006) exploring relationship banking, lending technologies, etc; hence the somewhat heavy reliance on the work of these two authors. They have described relationship banking as “one of the most powerful technologies available to reduce information problems in small firm finance” (Berger & Udell, 2002, p. F32).

An addition to the above definition is clearly stated in Berger and Udell (2006). The addition is concerned with two things. One is the type of proprietary information qualified as “soft information” upon which lending is primarily based. The second is relationship-banking as a whole being one type of loan underwriting, or a lending technology as per the

taxonomy discussed above (Table 1), among other loan underwriting technologies.

The relationships between the bank, the entrepreneur and the SME become more important than the pure financial condition of the company (Berger & Udell, 2003). The bank bases its decisions regarding the approval or refusal of a loan application from its SME partner, and the interest rate to charge, largely on proprietary information about the firm, its owner, and its community. This information is garnered partly in the course of the relationship through the provision of loans (Berger & Udell, 1995; Petersen & Rajan, 1994) deposits services (Allen, Saunders, & Udell, 1991; Berlin & Mester, 1999; Cole, 1998; Degryse & Cayseele, 2000; Nakamura, 1993), or the delivery of other financial services to the firm and/or to the entrepreneur. Specifically, “Deposit accounts provide further information in the form of balance information, transactions activity, payroll data, etc. that help give a more complete picture of the financial health of the firm. Information about the quality of the entrepreneur may also be culled from the provision of personal loans, credit cards, deposit accounts, trust accounts, investment services, etc., and from other business dealings or personal contact[s] outside the firm. Knowledge of the local community gained over time may also be

valuable because it allows the bank to judge the market in which the business operates, to obtain references and feedback on borrower performance, and to evaluate the quality of the firm's receivables” (Berger & Udell, 1998, pp.645-6).

Further information may also be collected from contact with the borrower’s customers and suppliers who may give specific information about the firm and owner or general information about the business environment in which they operate (Berger & Udell, 2002).

Finally, two remarks about how relationship banking is generally defined in the finance literature. First, more dimensions of this relationship have been added to the definition by different authors depending on the area of relationship banking under study. An example of this is Elsas (2005) where relationship lending is defined as “a long-term implicit contract between a bank and its debtor...” (p. 34). Secondly, it must be noted that all these definitions are from a bank’s perspective. That is, banks are the only active players according to these definitions and the business partner’s role is viewed as being passive. Maque (2007) arrived at the same conclusion in her PhD dissertation. Freixas (2005) seems to have touched on this issue. This might point to a gap about the definition of relationship banking in the finance literature.

### **II.6.2 Soft information:**

A distinguishing feature of the lending technologies involving relationship banking is the type of information, soft and/or hard, that is primarily used to underwrite a loan. Stein (2002) defined soft information as information that cannot be directly verified by anyone other than the agent who produces it and it cannot be unambiguously documented and passed on to someone else.

Soft information tends to be private information, not publically available, not normally asked for, and it must be voluntarily transferred in an exchange. More precisely, the sort of information referred to here is specific and non-standard information; firstly about the firm, such as unpublished strategies of the firm, inside management problems, succession problems, critical supplier or customer dependencies; secondly about the firm's owner/manager's business acumen or capability, such as his management ability, financial understanding, and his integrity; and lastly, information related to the firm's environment in terms of suppliers and customers (Berger & Udell, 2006).

Petersen (2004) talked about specific characterisations of hard and soft information. Whereas hard information is easily reduced to numbers and

is almost always recorded as numbers, soft information is difficult to completely summarise in a numeric score and is often communicated in text. The fact that hard information is quantitative means that it can easily be collected, stored and transmitted, thus the way in which it is collected is also different. This is because hard information is often reported through standard instruments such as financial statements, company reports and regulatory filings. By definition the collection methods for hard information need not be personal, whereas the collection methods for soft information must be personal.

Another difference is that hard information is also more comparable. The person in charge of collecting this kind of information can, and often will, be different from the person (or object) that evaluates the information and makes a decision. A firm's debt ratio is an example of hard information. There is a general agreement as to what a 1/2 debt ratio means for a firm, however, if you describe the owner of the firm as honest and a hard worker, there is less agreement about what honest and hardworking means (or how much these attributes are worth), because the interpretation of such adjectives is different from one person to another (Petersen, 2004).

In addition, with soft information, the context under which it is collected and the collector of the information are part of the information. It is not possible to separate the two. This is why soft information is collected in person and, historically, the decision maker is the same person as the information collector. “A typical example is a relationship-based loan officer. The loan officer has a long history with the borrower and, based on a multitude of personal contacts, has built up an impression of the borrower’s honesty, credit worthiness and likelihood of defaulting. Based [partly] on this view of the borrower and the loan officers’ experience, the loan is approved or denied” (Petersen, 2004, pp. 7-8).

The impact of this soft private information is distinctive in that it helps the lender identify where the firm’s expertise and dependencies reside, and the transfer of it props up the value creation in exchanges “by revealing to exchange partners the unique possibilities they possess for matching their competencies and resources...Hence, the solutions prompted by the transfer of private knowledge are valuable not only because they are distinctive, but also because they are hard for competitors without private knowledge to imitate” (Uzzi, 1999, p. 483).



## II.7 Benefits of relationship banking:

In line with the research gap detailed earlier in the ‘gap identification and motivation of the study’ section (I.2), this section identifies some of the benefits accruing to banks from relationship banking that constituted the starting point of investigation for this thesis.

It is clear from the scant and scattered theoretical literature on SME-bank relationships and the benefits accruing to banks that a number of benefits<sup>5</sup> accrue to banks from using the relationship banking model/technology to manage their relationship-managed SME clients. These value creation benefits are the ultimate rationale for relationship banking, and give banks – the users of relationship model/technology - a clear comparative advantage over other financial intermediaries that are non-users of the relationship model/technology when underwriting loans to SMEs. These benefits are summarised in Table 2 (below), and discussed thereafter.

---

<sup>5</sup> The same thing can be said about large businesses as well, but since the focus here is on small businesses, no attempt is made to discuss the case of large businesses.

Table 2: benefits of relationship banking accruing to banks

Relationship Benefit	Problem
<ul style="list-style-type: none"> <li>- Mitigation of the information asymmetry <ul style="list-style-type: none"> <li>• Useful method of investment and prospect evaluation</li> <li>• Continuous monitoring</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>- Agency relationship between bank &amp; SME client <ul style="list-style-type: none"> <li>• Adverse selection</li> <li>• Moral hazard</li> </ul> </li> </ul>
<ul style="list-style-type: none"> <li>- Reduction in the marginal cost of information production</li> </ul>	
<ul style="list-style-type: none"> <li>- Interaction over multiple products &amp; over time as source of information</li> </ul>	<ul style="list-style-type: none"> <li>- Information opacity</li> </ul>
<ul style="list-style-type: none"> <li>- Generation of information not available otherwise</li> </ul>	
<ul style="list-style-type: none"> <li>- Assessment of intangible assets</li> </ul>	<ul style="list-style-type: none"> <li>- Information opacity</li> </ul>
<ul style="list-style-type: none"> <li>- Use information collected to gain a comparative advantage in timing of offers</li> </ul>	<p>Increase return</p>
<ul style="list-style-type: none"> <li>- Get help with the proper interpretation of information provided by the SME</li> </ul>	<p>Information opacity</p>
<ul style="list-style-type: none"> <li>- Gain access to a SME niche market</li> </ul>	
<ul style="list-style-type: none"> <li>- Lower risk of Error type I &amp; II</li> </ul>	<p><i>Type I error</i> here refers to the case where a loan application would be declined when in reality it <u>should have been accepted</u> and the loan granted.</p> <p><i>Type II error</i> is when a loan application is accepted and the loan granted when the loan application <u>should have been declined</u>.</p>

While some of these benefits can be secured at least partly from using other lending technologies, that shouldn't be used as a counter argument to attribute these benefits to relationship banking. To do a proper assessment of relationship banking models every benefit must be included.

The first major advantage is the contribution the relationship makes towards alleviating the significant problems that arise from the agency issues between the bank and its SME client (Boot & Thakor, 1994; Thakor, 1995). An information wedge between the SME and its bank is created due to the information asymmetry where the SME borrower is more likely to have more information about the project, the subject of the loan, than the bank. This information wedge is mitigated through the relationship built between the two parties over time and multiple products supplied by the bank to the SME client (Petersen & Rajan, 1994).

Furthermore, relationship banking has been shown to be useful in overcoming the problems of adverse selection and moral hazard, as it allows for a better and more enhanced method of investment and prospect evaluation for the bank when approached by one of its SME clients for a loan (Bhattacharya & Chiesa, 1995; Boot, 2000; Diamond, 1991). Relationship banking also allows continuous monitoring by the bank of the SME's activities, ensuring that the funds are used for the purpose they were initially borrowed (Rajan & Winton, 1995), and stops the owner-manager from "indulging in [a] pet project, shifting risk

toward the bank, or otherwise misusing the borrowed funds” (Petersen & Rajan, 1994, p. 4).

Another benefit of relationship banking is reduction in the marginal cost of information production. This reduction is achieved through increased firm-specific information which the bank is able to use multiple times during the relationship period when providing the same and/or other financial services (Peltoniemi, 2007). The multiple use of information or information reusability takes two forms (Greenbaum & Thakor, 2007, p. 46). *Cross-sectional reusability* is the first form. The bank utilises the same information collected earlier about one of its clients either across a number of other clients and/or when the bank is processing another application from the same customer but across a number of other products and services. The second form is *inter-temporal reusability* whereby “for example, a bank that learns something about a borrower while processing its first loan application can use at least some of that information in processing future credit requests from the same borrower” (Greenbaum & Thakor, 2007, p. 46).

Interaction over multiple products and services via cross-selling bank products and the interaction over time represent a valuable source of information about the SME client (Degryse & Cayseele, 2000),

particularly when the information opacity associated with SMEs is taken into consideration. These other financial services or products include letters of credit, payrolls, cash management services, and/or deposits. In turn, this repetitive interaction over products and over time would (i) increase the bank's assessment precision about the firm and, (ii) allow the bank to "spread any fixed costs of producing information about the firm over multiple products" (Petersen & Rajan, 1994, p.6) which would also, (iii) reduce the bank's costs of providing more loans and services.

Generation of information that otherwise would not be available is another benefit cited by Berger and Udell (1998), Boot (2000), and Cole (1998). This is achieved through the bank having access to the firm's account movements and being able to "obtain sufficient information on the firm's ability to service debt-like claims by observing its past interactions with other fixed claim holders like employees or prior creditors" (Petersen & Rajan, 1994, p. 6).

Having relationship banking structure/arrangement/configuration with the SME owner/manager is the only method of assessing the SME's intangible assets, such as the owner-manager skills and character, intergenerational transfer of management roles, and continuity of the firm

(Holmes et al., 2003). These intangible assets are a valuable source of information as inputs to the credit approval process.

Using the information, soft and hard, private and public, secured from these multiple interactions, over time, over products, and with the SME owner/manager, the relationship bank partner would learn when to offer extra services and secure extra profits which would give it a comparative advantage over other finance providers.

Relationship banking provides the bank with the ability to better understand and correctly interpret the information provided by the SME owner/manager(s), particularly through the financial statements, and/or to check the accuracy of that information (Boulanouar, 2003). Boulanouar (2003) investigated the SME-bank relationship in Japan's Hiroshima area and found that banks using relationship lending technology actively sought direct input from small firm owners/managers ex-ante and ex-post in order to aid in the proper evaluation of the loan applications. The relationship technology also helped banks to inform and explain the evaluation process and outcomes, especially when applications were unsuccessful.

The relationship banking technology/model can help banks get into the lucrative SME borrower market. When lending to SMEs, the full use of standard evaluation methods of loan applications is not possible because “the numbers or the hard information may not tell the entire story” (Scott, 2006, p.544). This is because SMEs tend not to have audited financial statements, or have incomplete ones, and perhaps have short operating histories, etc. However, the private information acquired via the relationship medium would allow the bank to write contracts and extend loans that would not take place in the absence of this private information (Berlin & Mester, 1999; Bhattacharya & Chiesa, 1995; Rajan & Winton, 1995).

Relationship lending technology is characterised by the use of soft information which is collected by the loan officer in charge of managing the bank-SME relationship. Based on this soft information; “a bank could decide the owner is not very adaptable in the face of a new competitive threat, and, despite acceptable financial performance, turn down the next loan as a result of this soft information.... The bank could become aware of an impending change of control from an intergenerational transfer, a revised assessment of control systems that are inadequate to support growth (that could lead to fraud), or unexpected

health problems for an owner that lacks management depth - all factors that might lead to turndown” (Scott, 2006, p. 546).

## Conclusion

This chapter has set the scene for the thesis showing how banks are confronted with some challenges and issues when lending to SMEs and how banks try to overcome these. Particular emphasis was made on the role of relationship banking, with the chapter concluding with a review of literature on relationship banking benefits accruing to banks. The next chapter deals with the methodology utilised to investigate the research aim and questions.



### **III. Methodology**

#### **Introduction**

Choosing a research methodology and method depends on the researcher's understanding of the topic at the time of starting the investigation. This chapter details the different aspects of the qualitative research method used in this thesis. Beginning with the story of this research, the next section elaborates on how this research was initiated but eventually employed a qualitative approach. The following section makes the case for the use of a qualitative approach to the study. Particular attention is given to the relationship between qualitative research and casual explanation as per Miles and Huberman (1984) and also process theory and variance theory (Mohr, 1984). This is followed by an elaboration on the research design and finally the method of analysis is detailed.

#### **III.1 Organic underpinnings of this study:**

This study began to be formulated in late 2007. The original research topic was the gap identified by Boot (2000) in the area of relationship banking benefits accruing to banks.

Initially, after the gap in the knowledge was identified, the groundwork for a standard/orthodox (i.e. quantitative) way of approaching the topic was initiated in the same way other studies had been designed, such as those of Bharath et al. (2007); Puri et al. (2011). A primary research hypothesis was developed. The research hypothesis was: loans contracted through relationship banking have/enjoy lower rates of default than loans contracted/underwritten through business brokers. In New Zealand, some SMEs commonly approach business brokers to arrange their business borrowings (Ministry of Economic Development, 2003a). This was to test for, and measure, the benefits of relationship banking in the form of better screening of borrowers and investment and prospect evaluation (Bhattacharya & Chiesa, 1995; Boot, 2000; Diamond, 1991), and monitoring the use of borrowed funds (Petersen & Rajan, 1994; Rajan & Winton, 1995). Indeed a study with similar hypothesis was later conducted in the context of retail customers in Germany, thanks to access to private data (Puri et al., 2011). When different banks were approached for data to test this study's hypothesis, they all politely declined. However, four critical points led to a decision to stick with relationship banking and its benefits to banks and to instead change the research approach rather than change the topic. The four points were:

1. The gap in the literature identified above, and the research questions subsequently developed, were judged to be very important and worth pursuing.
2. Additionally, after speaking to several bankers, the author noticed hints to other substantial benefits of relationship banking accruing to banks not mentioned in the academic and trade literature. Other observations concerned issues such as the definition of relationship banking to bankers, and in combination these points hinted to considerations somewhat different from those reported in the literature.
3. Further, upon revisiting the identified gap in the literature by Boot (2000) as detailed in the gap identification section, the realisation that the opportunity for a contribution of the thesis existed in not just what the benefits were *but how* banks operationalized them, coupled with extensive reading on research methods such as Ardalan (2008); Johnson, Curran, Duberley, and Blackburn (2001); Maxwell (2004b, 2005); Miles and Huberman (1994); Yin (2003b) and much reflection allowed a different design to be considered. To address this gap, quantitative data collection was deemed impractical (bankers refused) but also superficial, i.e. did

not give the depth or breadth of data required to answer the subsequently developed research questions.

4. Finally, and most importantly, the author realised that the detailed research questions related to identification of the precise sources of value or benefits for banks and how banks secure these benefits were going to be better served/investigated by a qualitative research approach. This last point is further detailed in the coming section.

### **III.2 General case for the qualitative approach**

There are two general overarching approaches to research (Blumer, 1956; Maxwell, 2004b; Mohr, 1982; Ragin, 1989; Yin, 2003a). Mohr (1982) labels these approaches variance theory and process theory. With variance theory the (quantitative) researcher is interested in *whether*, and to *what extent*, variance in x causes variance in y. This approach has been illustrated in work relevant to relationship banking by Bharath et al. (2007); Puri et al. (2011) concerning benefits accruing to banks. However, with process theory the (qualitative) researcher asks *how* x plays a role in causing y, and what the process is that connects x and y (Maxwell, 2004b). Part of the misunderstanding about the use of qualitative and quantitative research approaches in dealing with causal

explanations has been the “failure to recognize that quantitative and qualitative researchers tend to ask different kinds of causal questions” (Maxwell, 2005, p. 23) as demonstrated by the structures of the variance and process theories.

Other researchers have made the same distinctions but have used different labels such as ‘variable analysis’ and the ‘process of interpretation’ (Blumer, 1956), ‘variable and case oriented approaches’ (Ragin, 1989), and ‘factor theories’ and ‘explanatory theories’ (Yin, 2003a). ‘Variable analysis’, ‘variable oriented approach’ and ‘factor theory’ are the same as variance theory, whereas ‘process of interpretation’, ‘case oriented approach’, and ‘explanatory theory’ are the same as process theory.

In qualitative research, emphasis [is] on understanding processes and mechanisms, rather than demonstrating regularities in the relationships between variables, therefore demonstration of causation is achieved via a description of sequence of events, each event flowing into the next. Quantitative studies, however, support an assertion of causation by showing a correlation/association between an earlier event and a subsequent event (Weiss, 1994) with what goes on in between explained by either theory or guesswork.

In other words, process theory “deals with events and the processes that connect them; it is based on an analysis of the causal processes by which some events influence others”. Process explanation, since it deals with specific events and processes, is less amenable to statistical approaches. “It lends itself to the in-depth study of one or a few cases or a ‘relatively small’ sample of individuals, and to textual forms of data that retain the chronological and contextual connections between events” (Maxwell & Loomis, 2003, p. 248).

Both variance theory and process theory are forms of causal explanation. “However, process theory is not merely ‘descriptive’, as opposed to “explanatory” variance theory; it is a different approach to explanation. Experimental and survey methods, “typically involve a ‘black box’ approach to the problem of causality; lacking direct information about social and cognitive processes, [researchers] must attempt to correlate differences in output with differences in input and control for other plausible factors that might affect the output. Qualitative methods, on the other hand, can often directly investigate these causal processes” (Maxwell, 2004b, p. 249).

Moreover, it is now widely accepted that a qualitative research approach is useful/beneficial for investigating local causalities (Flyvbjerg, 2006).

For example, Miles and Huberman asserted that “Until recently, the dominant view was that field studies should busy them-selves with description and leave the explanations to people with large quantitative data bases. Or perhaps field researchers, as is now widely believed, can provide ‘exploratory’ explanations—which still need to be quantitatively verified. Much recent research supports a claim that...field research is far *better* than solely quantified approaches at developing explanations of what we call *local causality*-the actual events and processes that led to specific outcomes” ((Miles & Huberman, 1994, p. 132, emphasis in original).

Consistent with the rise of these approaches that see, as Maxwell (2004b) notes, “causation as fundamentally a matter of processes and mechanisms rather than observed regularities” (p. 246) is the development of the distinction between variable and process oriented approaches to explanation.

Then, as a logical conclusion about which research methodology to use in the current study, as the interest lies in investigating the processes through/by which relationship banking benefits banks, rather than just investigating whether this relationship offers advantages, a qualitative research method is more appropriate.

This process approach to causation has been advocated by a significant number of qualitative researchers e.g., Britan (1978); Erickson (1986); Fielding and Fielding (1986); Schwandt (1997). For example, Sayer (2000) asserted that casual “explanation requires mainly interpretive and qualitative research to discover actors’ reasoning and circumstances in specific contexts – not in abstraction from them” (p. 23). This point, concerning context, is elaborated on in detail in section III.5 below.

Therefore, an in-depth understanding of the phenomenon under study within its overall context is essential. The processes which transpire between the different parties to a relationship cannot be “captured in hypothetical deductions, covariances, and degrees of freedom. Instead, understanding social process[es] involve getting inside the world of those generating it, and constructing an interpretation of 'other people's constructions of what they and their compatriots are up to” (Geertz, 1973, p. 9 as cited in Rosen, 1991, p. 8) . Similarly, as Rosen (1991) notes “nuance and uniqueness are as important in this endeavour as is normally frequent behaviour” (p. 8). Of necessity then, a researcher must involve him/herself in the world of those carrying out the events and processes in order to properly understand them. Interviewing the relationship



managers was the key to that, and interviews offer all of those necessary conditions to answer the thesis questions.

Qualitative researchers have demonstrated how using a process type of approach can be used to develop causal explanations in the sense of Miles and Huberman's statement "the actual events and processes that led to specific outcomes" (Miles & Huberman, 1984, p. 132). One such way is through qualitative interviews. Weiss (1994) maintained that: "In qualitative interview studies the demonstration of causation rests heavily on the description of a visualizable sequence of events, each event flowing into the next. ...quantitative studies support an assertion of causation by showing a correlation between an earlier event and a subsequent event. An analysis of data collected in a large-scale sample survey might, for example, show that there is a correlation between the level of the wife's education and the presence of a companionable marriage. In qualitative studies we would look for a process through which the wife's education or factors associated with her education express themselves in marital interaction" (Weiss, 1994, p. 179).

In-depth interviews "enable researchers to gain a rich understanding of respondents' perspectives, often providing insights that the researcher would not have uncovered from structured questionnaires used in

traditional surveys" (Osland & Cavusgil, 1998, pp. 200-201) and/or quantitative studies such as those investigating the association between the presence of relationship banking and the increase in cross selling of bank's products and services.

While loan applications from small businesses are evaluated using the different lending technologies referred to earlier (in section II.5), banks do not yet specify the amount of input from each lending technology used towards the final decision about a loan request. Hence the ability to segregate the benefits stemming from the use of relationship banking technology alone and using a quantitative approach to investigate the advantages of relationship banking to banks would be "extremely difficult to verify because currently available data do not identify how commercial loans are underwritten" (Udell, 2008, p. 98). Studies such as those of Bharath et al. (2007) and Ergungor (2005) don't seem to have dealt with how the lending process is done.

To be able to specify the contribution of each lending technology to the overall decision regarding a specific loan application, it is necessary to detail the lending process as well as the contribution of each of the lending technologies used. However in this thesis, the aim is to (separately) study the value creation and value addition of relationship

banking technology from the value creation and value addition of the other lending technologies used in order to get as close as possible to the true sources of the value of relationship banking, how that works, and how banks secure these value additions. These are made possible by taking a qualitative research approach as argued above.

### **III.3 Research method: Case study**

This study uses a case study research strategy. The case study has been identified as the most suitable research strategy as from its definition, it is as “an empirical inquiry that investigates a contemporary phenomenon within its real-life context” (Yin, 2003b, p. 13) and it deals with a situation where a “descriptive question (what happened?) or an explanatory question (how or why did something happen?)” (Yin, 2006, p. 112) are being asked. Case study method is recommended as a research strategy for research projects with three conditions (Yin, 2003b, pp. 1-2).

1. When investigating ‘why’ [use relationship banking] and ‘how’ [relationship banking benefits are secured i.e. process] questions because, as Yin (2003b) notes, “‘how’ and ‘why’ questions are more explanatory and likely to lead to the use of case studies... as the preferred research strategies”. The reasoning behind this is that

“such questions deal with operational links needing to be traced over time, rather than mere frequencies or incidence” (Yin, 2003b, p. 6), i.e. dealing and appreciating processes.

2. Case study method is preferred in examining contemporary events where the relevant behaviours cannot be manipulated (Yin, 1994) [that is use of different lending technologies in tandem where control over the contribution of each technology is not able to be segregated], and
3. Three, when the sample under study exists as a contemporary phenomenon, or more precisely it's an explanatory case study complemented by a descriptive (including casual) inquiry (Yin, 2003b).

The case under study is relationship banking benefits from the bank's side, with the small business-bank relationship in New Zealand as the context and descriptive questions being asked about the phenomenon, why it happens and how it happens. The purpose of this format is to empirically investigate and gain a comprehensive understanding of the relationship benefits to banks.

Furthermore, as Osland and Cavusgil (1998), state “in depth case studies have been determined to be an effective approach when investigating

dynamic organisational processes...and in creating theory that incorporates the participants' constructs and frameworks, rather than the researcher's" (p. 194). Therefore, this format also facilitates the thesis's aim of investigating the relationship banking benefits and the processes used to secure them incorporating the interviewees' (relationship banking managers in this case) inputs on how those processes actually happen.

Further advantages of using the case study as a research method have been reported in the literature. Some of these advantages are: the researcher can control the scope and time of the examination, allowing the researcher to gain primary data within a controllable timeframe; examining the phenomenon of interest in a natural setting from the perspective of the participants allows the researcher to understand the dynamics that are present (Eisenhardt, 1989). This method may help explain the links in real-life governance interruptions that are too complex for a survey or experimental strategies (Yin, 1994). A further advantage of adopting the case study method of research is that it has the potential to provide a creative insight that may arise from the comparison of contradictory or paradoxical evidence (Cameron & Quinn, 1988).

So, taking together the case study method and process theory format as this study does will help to answer the main aim of the thesis which is to

investigate the processes of securing the benefits of relationship banking to banks.

#### **III.4 Criticism of the case study method/approach:**

Notwithstanding the advantages that case studies offer as a research method, some issues have been raised. Since ‘generalisability of the case study’ is one of those issues which is relevant to this thesis, the rest of this section will deal with it in the context of this study.

When the concept of generalisation is applied to case studies a misunderstanding of the objectives of this type of research can result in the wrong questions being asked, in the same way that the disagreement on whether process theories can adequately address issues of causation can be attributed to a “failure to recognize that quantitative and qualitative researchers tend to ask different kinds of causal questions” (Maxwell, 2005, p. 23) as explained in section III.2 above. The objective from the use of case studies is not a universal generalisation but a deeper and a more formal understanding of the phenomenon (identification of the precise sources of value creation and value addition of relationship banking to banks) in a single setting (New Zealand) within its context (New Zealand banking) from the participants’ (banks’ relationship managers) perspective. In this way, an inside understanding not the

singular understanding is generated (Flyvbjerg, 2006). The understanding generated from the single setting studied can then be used as a template in other settings to test for generalisation and replication and to see if the shared elements of that understanding exist across all settings, and/or to what degree.

Furthermore, the thesis's aim is structured in a such way, i.e. what are the relationship banking benefits to the five... and “how do the five main bank brands in New Zealand secure benefits of relationship banking when dealing with their relationship managed small businesses clients”, because as Maxwell (2005) has stated “a qualitative study can confidently answer such a question posed in particularistic terms [because] this way of stating the question, although it does not avoid issues of sampling<sup>6</sup>, frames the study much more in ‘case’ terms” (p. 71). The five main bank brands are treated not as a sample from some much larger population of banks to whom the study is intended to generalise, but as a case of a group of banks that are studied in a particular context, New Zealand. The selection of a particular case may involve considerations of representativeness, but the primary concern of the study is not with generalisation, it is with developing adequate descriptions,

---

<sup>6</sup> For a discussion of sampling issues please see sections III.6.1 and III.6.2 below.

interpretations, and explanations of this case (Maxwell, 2005) in order to investigate the processes these banks in New Zealand use to secure relationship banking benefits.

Other methodologists have argued for taking a different perspective on generalisability within the case study framework and four of these perspectives, those of Orlikowski and Baroudi (1991), Bryman (1988), Yin (2003b), and Flyvbjerg (2006) will be considered in turn.

The thesis aim is to seek a relative, albeit shared, understanding of phenomena. Generalisation from a single case study setting “to a population is not sought; rather, the intent is to understand the deeper structure of a phenomenon, which it is believed can then be used to inform other settings” (Orlikowski & Baroudi, 1991, p. 4).

Bryman (1988) agrees that “The problem of case study generalization entails a misunderstanding of the aims of such research. In particular, [the] misconception arises from a tendency to approach a case study as if it were a sample of one drawn from a wider universe of such cases. There are at least two reasons for considering this view to be misguided.” One of which is the “issue is better couched in terms of the generalisability of



cases to theoretical propositions rather than populations or universes” (1988, p. 90).

Yin (2003b) perspective deals, on the other hand with the issue of ‘case studies providing little basis for scientific generalisation’ by tackling the frequently heard question: How can you generalize from a single case? For Yin (2003b), case studies are like experiments and “scientific facts are rarely based on single experiments; they are usually based on a multiple set of experiments that have replicated the same phenomenon under different conditions” (p. 10). In conclusion then, the same approach can be used with multiple case studies, and like experiments, case studies “are generalisable to theoretical propositions and not to populations or universes. In this sense, the case study, like the experiment, does not represent a ‘sample’, and in doing a case study, the goal will be to expand generalised theories (analytic generalisation) and not to enumerate frequencies (statistical generalization)” (Yin, 2003b, p. 10).

Finally, the author of this thesis is in full agreement with the following “Finally, it should be mentioned that formal generalization, be it on the basis of large samples or single cases, is considerably overrated as the main source of scientific progress. Economist Mark Blaug (1980) – a

self-declared adherent to the hypothetico-deductive model of science – has demonstrated that while economists typically pay lip service to the hypothetico-deductive model and to generalization, they rarely practise what they preach in actual research. More generally, Thomas Kuhn has shown that the most important precondition for science is that researchers possess a wide range of practical skills for carrying out scientific work. Generalization is just one of these. In Germanic languages, the term ‘science’ (Wissenschaft) means literally ‘to gain knowledge’. And formal generalization is only one of many ways by which people gain and accumulate knowledge. That knowledge cannot be formally generalized does not mean that it cannot enter into the collective process of knowledge accumulation in a given field or in a society. A purely descriptive, phenomenological case study without any attempt to generalize can certainly be of value in this process and has often helped cut a path towards scientific innovation. This is not to criticize attempts at formal generalization, for such attempts are essential and effective means of scientific development. It is only to emphasize the limitations, which follows when formal generalization becomes the only legitimate method of scientific inquiry” (Flyvbjerg, 2006, p. 227).

In light of the above arguments and as Alasuutari (1995), Bryman (1988), and Silverman (2005) suggested, extrapolation is a more appropriate

concept than generalisability in this case because it demonstrates how the analysis of this thesis, and its findings, relate to other contexts about studies on value creation and the value of relationship banking benefits accruing to banks.

In summary, while this study does not seek to provide empirical generalisations of its outcomes across all relationship banking contexts, it does meet the aim of providing testable constructs (benefits and their sources) which can then be tested in other contexts.

### **III.5 The importance of the Context**

As was mentioned earlier this study's paradigm is realist and as noted in section III.2 (above) that for social realist researchers context plays an important role in causal explanation (Miles & Huberman, 1984; Sayer, 2000). This position has been summed up by Pawson and Tilley (1997) as "mechanism + context = outcome" (p. xv) where it is maintained that "the relationship between causal mechanisms and their effects is not fixed, but contingent" (p. 69).

So, the causal relationship depends on the context in which the mechanism operates. The context within which a causal process occurs constitutes, to some extent, an inherent part of that process, and often

cannot be “controlled for” in a variance-theory approach without the misrepresentation of the causal mechanism (Sayer, 2000).

Furthermore, emphasis on context is critically important for the generalisation of causal statements as noted by the National Research Council (U.S.): “Attention to context is especially critical for understanding the extent to which theories and findings may generalize to other times, places, and populations”(NRC, 2002, p. 5). This view treats context as one source of “noise” that “make[s] replication—the key to boosting certainty in results and refining theory—more difficult and nuanced” (NRC, 2002, p. 83) in social and behavioural research.

From this thesis’s perspective, in order to develop adequate explanations of the relationship banking benefits accruing to banks, and also to understand the mechanisms leading into the securitisation of those benefits, methods need to be used “that can investigate the involvement of particular contexts in the processes that generate these phenomena and outcomes” (Maxwell, 2004a, pp. 6-7).

This is, in part, why a separate chapter 0 (below) on New Zealand banking and SMEs in New Zealand is positioned after the methodology chapter. The purpose is to show that the New Zealand context has been carefully chosen and to ensure it contains all the necessary elements of the phenomenon under study.

### III.6 Case study components

In one of the most recent studies available, Thomas (2011) defines case studies as “analyses of persons, events, decisions, periods, projects, policies, institutions, or other systems that are studied holistically by one or more methods. The case that is the subject of the inquiry will be an instance of a class of phenomena that provides an analytical frame—an object—within which the study is conducted and which the case illuminates and explicates” (p. 515).

Thomas (2011) notes that for a research project to constitute a case study, it must comprise two elements: the subject or case<sup>7</sup> of the study and its object. He also stresses that the difference between the case of a case study and its object is critical and must be made at the start “since the distinction between the one and the other is characteristic of all social inquiry, yet relatively neglected in discussion of the case study.” This is because “The ostensible looseness of the case study as a form of inquiry and the conspicuous primacy given to the case (the subject) is perhaps a reason for inexperienced social inquirers, especially students, to neglect to establish any kind of object (literally and technically) for their inquiries. Identifying only a [case], they fail to seek to explain anything,

---

<sup>7</sup> As the majority of writings on case studies refer to subject as case, from now on I will be referring to the subject as a case.

providing instead, therefore, a simple description in place of a piece of research” (p.513).

The case of a case study is defined as “a practical, historical unity” (Thomas, 2011, p. 513), which George and Bennett (2005) detail as “the universe—that is, the ‘class’ or ‘subclass’ of events—of which a single case or a group of cases to be studied are instances” (p. 69).

The object, to Thomas (2011), is defined as “an analytic or theoretical frame” (p.513); hence “the object constitutes, then, the analytical frame within which the case is viewed and which the case exemplifies” (Thomas, 2011, p. 515).

It is worth noting that other authors, such as Wieviorka (1992) and Wallace (1969), have also stressed the difference between object and subject (in the language of Thomas (2011)) of different types of research, though utilising different terms. Wallace (1969) for example used the terms explanandum<sup>8</sup> and explanans to mean case and object respectively, with explanandum meaning the phenomenon that needs to be explained and explanans the thing doing the explanation (of the phenomenon). This

---

<sup>8</sup> An explanandum (a Latin term) is a phenomenon that needs to be explained (i.e. that which needs to be explained", plural = explananda -Online dictionary of philosophy-) and its explanans is the explanation of that phenomenon. For example, one person may pose an explanandum by asking "Why is there smoke?", and another may provide an explanans by responding "Because there is a fire". In this example, "smoke" is the explanandum, and "fire" is the explanans.

discussion about the case study, its subject and its object, in relation to the current thesis, can be summarised in the following Table 3 (below).

**Table 3: the case study, its subject, and object**

Case: practical, historical unity Explanandum: The thing to be explained	Object: analytical/theoretical frame Explanans: The thing doing the explaining	Case Study
The five main bank brands in NZ	‘The process of securing relationship banking benefits to banks’	So: the ‘5 main banks in NZ’ as a case study of ‘Process of securing relationship banking benefits to banks’

### **III.6.1 Selection of the case “banks”:**

Having identified the parameters of a case and object, the next task is the identification of the case of the case study. The case will be “selected because it is an interesting or unusual or revealing example through which the lineaments of the object can be refracted” (Thomas, 2011, p. 514). This, however, can only be achieved through purposive sampling of a case or cases. This method of sampling allows the researcher “to choose a case because it illustrates some feature or process in which [s/he is] interested” (Silverman, 2009, p. 141). Also, this method of sampling demands the researcher to “think critically about the parameters of the population [s/he is] interested in and choose [the] sample case[s] carefully on this basis” (Silverman, 2009, p. 141). Denzin and Lincoln (1994) agree, stating that “many qualitative researchers employ...purposive, and not random, sampling methods. They seek out

groups, settings and individuals where...the processes being studied are most likely to occur” (p. 202). This is so because the aim of the study is not to describe the symptoms of the relationship phenomenon and how frequently they occur, rather, and more importantly, it is “to clarify the deeper causes behind [it]...and its consequences” (Flyvbjerg, 2006, p. 229). The goal is not to representatively capture all possible variations but to gain a deeper understanding of the phenomenon and so the selection of case(s) to be studied should be done on the basis of its/their relevance to the researcher’s research questions, his/her theoretical position...and most importantly the explanation or account which s/he is developing (Mason, 2002).

Furthermore, “theoretical sampling is concerned with constructing a sample... which is meaningful theoretically, because it builds in certain characteristics or criteria which help to develop and test [the researcher’s] theory and explanation” (Mason, 2002, p. 124).

When information cannot be gathered as well from other choices, particular activities, people or settings may be deliberately selected. In fact, Weiss (1994) argued that ‘panels’ was a more correct term than ‘samples’ for many qualitative interview studies as “people who are uniquely able to be informative because they are expert in an area or were privileged witnesses to an event” (p.17) are utilised. “Selecting



those times, settings, and individuals that can provide [the researcher] with the information that [s/he] need[s] in order to answer [his/her] research questions is the most important consideration in qualitative selection decisions” (Maxwell, 2005, p. 88).

Finally, Mason (1996) recommendation is that to select a sample which can represent a wider population a sample needs to be selected “of particular processes, types, categories or examples which are relevant to or appear” (p. 92) to be so within that wider population or universe. “So in qualitative research the relevant or sampleable units are often seen as theoretically defined” (Silverman, 2009, p. 144). This is consistent with the aim of this thesis regarding the generalisability of cases being to theoretical propositions rather than populations or universes (Bryman, 1988) as explained in section III.4 (above).

Practically, the case selection was guided by Stake (2005) typology of cases where he distinguishes between three types of cases: intrinsic, instrumental, and collective or multiple.

An intrinsic case is examined for its intrinsic sake. For example, “why did bank ‘A’ fail to retain its small business clients when all other banks in the region succeed?” An instrumental case is examined primarily to provide insight into an issue. The case itself plays only a supporting role in understanding something else: an abstract construct or generic

phenomenon which the case illustrates. “The case is still looked at in depth, its contexts scrutinized, its ordinary activities detailed, but all because this helps the researcher to pursue the external interest. Here the choice of case is made to advance understanding of that other interest” (Stake, 2005, p. 445). For instance, how a community-bank X (representing other community banks in country ‘B’) manages to retain its small business clients.

In a multiple case study or collective case study, data is coordinated from a number of cases which are studied jointly so as to examine a phenomenon. Each case illustrates the same phenomenon, hence, a collective case study is an “instrumental study extended to several cases. Individual cases in the collection are [thus]...chosen because it is believed that understanding them will lead to better understanding, and perhaps better theorizing, about a still larger collection of cases” (Stake, 2005, p. 446). An example would be a collective case study of how three community-banks X, Y, and Z in country B manage to retain their small business clients.

Since the aim/interest of the current study is in banks that use relationship banking with their SME clients, the decision has been to select the five main bank brands in New Zealand. Therefore, this thesis identifies itself as a collective case study. The five main bank brands in

New Zealand exemplify the analytic frame, the object, which is the process by which banks operationalise relationship banking benefits to themselves. Hence, the five main bank brands in New Zealand, in Thomas (2011) words, are “the prism through which ‘facts and concepts, reality and hypotheses’ about this [process] were refracted, viewed and studied” (p.515).

The choice of those five bank brands is based on a number of criteria, two key ones are: one, together these banks control 83% of the registered banks’ total assets in New Zealand (Reserve Bank of NZ, 2008). This criterion reflects the importance of these banks in the New Zealand market in general and in particular, it represents a significant share of the small business market; and two, these banks use the relationship banking model with some of their small business clients. These two points are detailed further in the empirical context of the study in sections IV.2.3 below).

### **III.6.2 Selections of interviewees from within each bank:**

Purposive-expert sampling, another subcategory of purposive sampling, was also used to seek potential interviewees from within each of the selected banks. Purposive-expert sampling involves the selection of persons with known or demonstrable experience and expertise in some

area (Kuzel, 1999; Patton, 1990). It was used to “look for individuals who have particular expertise that is most likely to be able to advance the research’s interests, potentially open new doors” (Palys, 2008, pp. 697-698), and who are most conducive and accessible to gaining the understandings sought (Maxwell, 2012).

In the current study, specific qualifications, experience and practical knowledge in business/relationship banking was sought. Therefore, and in addition to looking at the organisational structure of the different banks (as well as the job description of) the people with the most practical knowledge of relationship banking and who are also responsible for implementing the banks’ relationship banking policies when dealing with their relationship managed SME clients, would be relationship managers. These positions are also referred to as loan officers (Scott, 2006), business managers, business banking managers (Ministry of Economic Development, 2003a), or business bankers (Colgate & Lang, 2005).

The banks’ relationship managers were considered to be the best potential interviewees as they are at the forefront of the banks dealing with the relationship-managed small business clients, and are also responsible for managing the relationship banking from the bank side (Ministry of Economic Development, 2003a). Relationship managers are

assigned to small business clients (Ministry of Economic Development, 2003a), thus occupying a position which is close to the SME client and acting as the point of contact with them (Colgate & Lang, 2005).

A job description of relationship managers - among other things - includes approving loans within their discretionary limits, communicating the banks' decisions to the SME clients in response to their loan applications (Ministry of Economic Development, 2003a). Relationship managers play a critical role in the production of, and interpretation of, soft information used to provide a more complete profile of the small business client for credit decisions assessment (Scott, 2006).

Furthermore, as relationship managers have a unique position as a repository of information about borrower performance, they know more about the SME borrower than any other person from within the bank. This is because of their critical role in the solicitation and negotiation of the loan. Therefore the relationship managers have an advantage in the assessment of any information about the subsequent performance of their SME borrower. Furthermore, the advantage is improved by the fact that the relationship managers maintain personal contacts with the SME borrowers (Udell, 1989).

In summary then, relationship managers are at the coalface of relationship banking with small business clients and thus are the mediating force/influence in driving the quality of the overall relationship banking (Colgate & Lang, 2005), are more likely to be aware of what type of information is needed to secure a specific relationship-banking benefit, how to obtain that information and how to use it to secure that specific benefit.

In addition to the purposive-expert sampling methods, and in line with the study being a collective case study, the interviewees were selected using an additional goal to obtain one interviewee from each bank in each of New Zealand's five major cities with the additional benefit of being able to see if they were any nuances and/or differences between the different areas. So, one business manager from each of the five main bank brands in each of the main cities (Auckland, Hamilton, Wellington, Christchurch, and Dunedin) was targeted.

The actual recruitment/selection of interviewees followed different paths. For Dunedin, relationship managers were contacted who had been involved in a previous study with the author, and were subsequently recruited. Additionally, the author was introduced to two regional managers from two different banks. Those two regional managers

accepted to participate in the study and one of them introduced the author to one of his relationship managers. The other regional manager helped with recruiting interviewees from his bank throughout four cities by sending an email to all their relationship managers. In the case of two banks, they provide the details of their relationship managers online (such as names, phone numbers and email addresses), allowing these relationship managers to be contacted and recruited directly. Lastly with one bank, a phone call was made to the bank call centre asking to speak to a relationship manager from each of the cities. Apart from one interviewee, who held the position of relationship strategy manager, all 26 interviewees were either relationship managers (21) or had worked as business managers previously and were still connected to the business of relationship banking management such as the regional/district manager to whom the relationship-managers report (Ministry of Economic Development, 2003a). Also, at the time of the interviews, five interviewees were working in senior positions, such as regional managers or, in one case, as a marketing manager for the whole bank.

<b>Years in the banking industry</b>	<b>Business manager position (in years)</b>	<b>Number of group of clients</b>	<b>Previous areas/expertise</b>	<b>Length of interview</b>	<b>Ge</b>
20	8	100	Personal banking	1:31:39	Ma

3	6 months	70 Asian businesses	Risk management, market risk, and commercial credit looking at loan applications	1:59:35	
Over 25	5	237	Branch manager for 15 years	2:15:33	
Over 33	19	Not applicable (n/ap)	Different areas of business and personal banking	1:59:53	
25	4	Not available (n/av)	Branch teller, batching, loan clerk, securities clerk, business manager assistant	1:46:40	Fem
10	6.5	90		1:27:10	
30 Years	n/av	n/ap	Different areas of commercial and corporate banking, coaching business managers etc	1:43:15	
30	10	400	Worked through the bank networks including at the loan processing office	1:52:51	
27	n/av	500+	Different areas	1:52:29	
5	1.5	300	Assistant commercial manager, institutional transactional banking, and personal lending at a branch level	1:08:57	
Over 35	15	n/ap	Corporate lending and business lending	00:42:17	
30	3		Different areas of personal and business banking	02:29:26	
10	8	90	Personnel and business banking	1:46:39	
6	3	n/av	Assistant manager then as trainee manager.	1:58:42	
30	Over 20	120	Bank teller, clerk helping out with loan applications.	01:39:54	
15	-	124	Personal and business banking	00:49:46	
33	2	325	Bank teller, team leader for personal banking team.	00:49:20	
23	12	300	Assistant manager then different levels of business banking.	00:54:46	
15	7	170	Bank branches then in the processing centres where business and personal loan applications are processed.	2:09:24	
8	No previous relationship management experience	n/ap	The strategy and planning department of Personnel banking. A business planning manager as part of the business banking team in head office.	1:05:23	
Over 35	-	n/ap	Most areas of banking: Dealer in the dealing room overseas, branch manager, commercial relationship	1:46:52	



			manager Lately specialised in the SME area, though has been involved with the SMEs his whole life in one way or another, more intensively last 5 years.		
24	8	220	Different levels of business banking	1:41:44	
18	5	170	Different areas of banking such as assessment of loan applications, business manager assistant, international operations Forex	1:53:43	
Over 25	Over 8	n/ap		1:14:59	
15	5	n/ap		1:38:01	
-	-	-		1:50:1	
Over 15	Over 10	n/av		~ 1:30:00	

Table

4

(below) summarises the interviewees' attributes as well as the interviews date and length.

<b>Interviewee number</b>	<b>Years in the banking industry</b>	<b>Business manager position (in years)</b>	<b>Number of group of clients</b>	<b>Previous areas/expertise</b>	<b>Length of interview</b>	<b>Gender</b>	<b>Interviews date</b>
<b>1</b>	20	8	100	Personal banking	1:31:39	Male (M)	27 Oct 09
<b>2</b>	3	6 months	70 Asian businesses	Risk management, market risk, and commercial credit looking at loan applications	1:59:35	M	14_July_09
<b>3</b>	Over 25	5	237	Branch manager for 15 years	2:15:33	M	9 July 09
<b>4<sup>9</sup></b>	Over 33	19	Not applicable (n/ap)	Different areas of business and personal banking	1:59:53	M	12 June 09
<b>5</b>	25	4	Not available (n/av)	Branch teller, batching, loan clerk, securities clerk, business manager assistant	1:46:40	Female (F)	25 June 09
<b>6</b>	10	6.5	90		1:27:10	M	17 July 09
<b>7<sup>10</sup></b>	30 Years	n/av	n/ap	Different areas of commercial and corporate banking, coaching business managers etc	1:43:15	M	9 Feb 10
<b>8</b>	30	10	400	Worked through the bank networks including at the loan processing office	1:52:51	M	14 July 09
<b>9<sup>11</sup></b>	27	n/av	500+	Different areas	1:52:29	M	15 June 09
<b>10</b>	5	1.5	300	Assistant commercial manager, institutional transactional banking, and personal lending at a branch level	1:08:57	F	17 Jul 09
<b>11<sup>12</sup></b>	Over 35	15	n/ap	Corporate lending and business lending	00:42:17	M	08 March 10
<b>12</b>	30	3		Different areas of personal and business banking	02:29:26	M	14 July 09

<sup>9</sup> A regional manager supervising 21 business managers and 19 assistant managers.

<sup>10</sup> Manages a team of mobile business managers.

<sup>11</sup> Based in a rural town.

<sup>12</sup> Managing the retail bank for a whole region's branches with about 700 employees.

<b>13</b>	10	8	90	Personnel and business banking	1:46:39	M	30 June 09
<b>14</b>	6	3	n/av	Assistant manager then as trainee manager.	1:58:42	M	16 July 09
<b>15</b>	30	Over 20	120	Bank teller, clerk helping out with loan applications.	01:39:54	M	28 Oct 09
<b>16</b>	15	-	124	Personal and business banking	00:49:46	M	17 July 09
<b>17</b>	33	2	325	Bank teller, team leader for personal banking team.	00:49:20	F	14 July 09
<b>18</b>	23	12	300	Assistant manager then different levels of business banking.	00:54:46	M	10 July 09
<b>19</b>	15	7	170	Bank branches then in the processing centres where business and personal loan applications are processed.	2:09:24	M	9 June 09
<b>20</b>	8	No previous relationship management experience	n/ap	The strategy and planning department of Personnel banking. A business planning manager as part of the business banking team in head office.	1:05:23	M	7_October_09
<b>21<sup>13</sup></b>	Over 35	-	n/ap	Most areas of banking: Dealer in the dealing room overseas, branch manager, commercial relationship manager Lately specialised in the SME area, though has been involved with the SMEs his whole life in one way or another, more intensively last 5 years.	1:46:52	M	08 March 10
<b>22</b>	24	8	220	Different levels of business banking	1:41:44	M	13 July 09
<b>23</b>	18	5	170	Different areas of banking such as assessment of loan applications, business manager assistant, international operations Forex	1:53:43	M	9 July 09

<sup>13</sup> Regional manager managing relationship managers.

<b>24<sup>14</sup></b>	Over 25	Over 8	n/ap		1:14:59	M	18 February 09
<b>25<sup>15</sup></b>	15	5	n/ap		1:38:01	M	3 March 09
<b>26</b>	-	-	-		1:50:1	M	16 July 09
<b>27<sup>16</sup></b>	Over 15	Over 10	n/av		~ 1:30:00	M	10 July 09

**Table 4: Interviewees attributes**

---

<sup>14</sup> An area manager with business managers reporting to him

<sup>15</sup> Branch manager managing personal and business managers

<sup>16</sup> Please note that interviewees 24 and 25 included in this table were pilot interviewees thus bringing the total to 27 interviews. More detail about the pilot interviews is provided in section III.7.4 Pilot interviews, below.

### **III.7 Development of the interview themes and questions**

As mentioned earlier, research interviews were found to be the best method of data gathering to aid answering the thesis's developed aim and for answering its research questions. Interviews are one of the most important methods of data collection in qualitative research (Myers, 1997; Qu & Dumay, 2011). King (1994), in capturing the very essence of the interview procedure stated that "the objective of interviews is —to see the research topic from the perspective of the interviewee and to understand how and why he or she comes to have this particular perspective (p. 14)." An objective of this study is to discover, from the relationship managers interviews, based on their own perspective and understanding, experiences of what relationship banking is, what the benefits to banks are, how they secure them, and how they go about scoring those benefits.

Interview types range from non-directive interviews to fully structured and defined questionnaires (Jones, 1985). Moreover, the nature of the thesis's aim - being investigating processes and looking at causal explanations - dictated the adoption of semi-structured and defined interviews to gather data (Easterby-Smith, Thorpe, & Lowe, 2002).

In preparing for the interviews, and to answer the research questions developed, a review of the literature as recommended by (Cooper, 1984) on the topics related to the thesis themes was undertaken,

starting from the general and moving down to the more specific. The themes included small business finance, banking in New Zealand, loan application assessments procedures, types of and sources of information used, reason (s) for using relationship banking, definition of relationship banking, its benefits, and process(es) of operationalisation. The purpose was to determine general themes which demanded investigation, to develop sharper and more insightful questions around those themes (Yin, 2003b), and to gain some precision in formulating those questions.

However, the groups of interview 'topics' or 'themes' developed were not meant to be definitive. This was because as data was gathered, an iterative process would see ideas added to the themes or adjustments made to them as appropriate (Walker, 1985).

Walker (1985) detailed this further, stating "in preparing for interviews a researcher will have, and should have some broad questions [in mind or on a checklist] and the more interviews they do, the more patterns they see in the data, the more they are likely to use this grounded understanding to want to explore in certain directions rather than others" (p. 47).

In other words, the interviews themselves informed each other and so were iterative in the sense that the 'flow' of the interview followed the ideas/interest of the respondent and each interview informed the next,

giving ideas of strands to pursue for more insightful information (Kvale, 2007; Walker, 1985; Weiss, 1994). The themes developed and explored in the interviews were structured around the thesis research questions.

### **III.7.1 Mapping the interview questions with the thesis research questions**

A critical distinction had to be made between the thesis research questions and the interview questions that were to be developed from the interview themes. This is referred to as translating the research questions into interview questions (Kvale, 2007). This is because the thesis's research questions identify and formulate what the researcher seeks to understand, whereas the interview questions are what the researcher asks his interviewees in order to gain that understanding (Maxwell, 2005).

So in preparing interview guides it is recommended to develop two interview guides, one with the thesis's main thematic research questions in academic language and another with interview questions to be asked “which takes both the thematic and the dynamic dimensions [of the interviews] into account. [The reason being that] the researcher questions are usually formulated in a theoretical language, whereas the interviewer questions should be expressed in the everyday language of the interviewees” (Kvale, 2007, p. 58).

Table 5 (below), depicts the translation of thesis research questions, first into the interview themes and then into the interview questions guide, providing correspondence between a sample of interview questions, interview themes, the thesis's research questions and its overall aim.

The interview questions included: what is relationship banking to business managers? How do they assess loan applications from their (typical) relationship-managed small business clients? What type of information do they seek from their small business clients? As business managers, how does relationship banking help them to get that information, and how? Does relationship banking with the small business client help? What are the benefits of relationship banking? More details of the questions posed in the semi-structured interviews are found in Appendix 3: Interview schedule IX.3 (below). The order and details of questions as they appear in the interview schedule is only indicative of the way the conversations were directed and does not reflect the actual order in which the questions were asked. This issue is explained further in section III.7.2 below.



**Table 5: Mapping of interview questions with interview themes and the thesis's aim and research questions.**

<b>Interview questions (samples)</b>	<b>Interview themes (samples)</b>	<b>The thesis's research questions</b>	<b>The Thesis's Aim</b>
What is relationship banking to you as relationship manager? And to you as a bank?	Definition of relationship banking.	1- What does relationship-banking mean to the five major bank brands in New Zealand?	To investigate the sources of benefits from relationship banking accrued by the five major bank brands in New Zealand when dealing with their SME customers and the processes/mechanisms for securing these benefits.
What drives you and the bank to build/have relationship banking with small business clients?	Motivation(s) for using relationship banking model.	2- What makes these five bank brands use a relationship banking model with their SME clients?	
How do you process a loan application from a relationship-managed SME client? Are there specific steps you follow? What are these steps you follow? Who gets involved? How, and why?	Process(s) of relationship banking building. Measuring strength of relationship banking...	3- How does the relationship-banking process actually work?	

<p>Is relationship banking beneficial?</p> <p>How?</p> <p>What are the benefits?</p>	<p>Benefits of relationship benefits to relationship managers and to banks.</p>	<p>4- What are the sources of value (i.e. benefits) of relationship banking to these five major bank brands when dealing with SMEs in New Zealand?</p>	
<p>How do you secure/scoop up those benefits?</p> <p>What do you use?</p> <p>What do you need?</p>	<p>Processes of securing the relationship banking benefits</p>	<p>5- How do these banks secure these benefits?</p>	

### III.7.2 Techniques to Improve quality of interviews:

Much useful advice on how to improve the quality of the interview process is detailed in the interviewing literature (King, 1994; Kvale & Brinkmann, 2009; Merriam, 1988; Whyte, 1982). This study's author tried as much as possible to adhere to that advice, some of which is detailed below.

Whyte (1982) emphasises the need to be careful not to interrupt an interviewee or to pass judgement on anything said during the course of the interview, though this does not mean questioning is not used when necessary or accepting everything that is said. King (1994) also cautioned the interviewer against imposing his or her perceptions on the interviewee either deliberately or subconsciously. A point by

Kvale and Brinkmann (2009) about this issue is to introduce themes to interviewees and let them elaborate.

It is also desirable for the interview to take the form of a professional conversation and is planned with a purpose to seek the interviewee's understanding of the phenomenon studied in a semi-structured interview style; reflexive interviewing techniques are recommended (Alvesson, 2003). Reflexive interviewing centres around the development of a dialogue between the researcher and the interviewee, and "once the interview assumes the form of dialogue the interviewee opens up and feels free to tell his/her story" (Alvesson, 2003, p. 245) with explanations providing the researcher with an opportunity to probe for information (Alvesson, 2003).

Regarding the use of probes, primarily, Qu and Dumay (2011) suggested the use of scheduled and unscheduled probes which would provide "the researcher with the means to draw out more complete narratives from the interviewees, drilling down a particular topic. A scheduled probe would require the interviewee to elaborate on a stimulating or surprising answer just made. For example, the interviewer endeavours to follow up immediately with a standard question, such as 'please tell me more about that [...]' when the interviewee suddenly discloses an area of great interest" (p. 247).

### III.7.3 Ethical approval:

The University of Waikato Ethics Committee guidelines were closely followed. Those guidelines<sup>17</sup> covered issues such as informed consent of participants, archiving of data, privacy, storage, and use of information. As required, ethical approval for the project was secured before any of the interviews were conducted. All interviewees were informed about the parameters of the ethical approval during the period of recruitment, and again before the start of the interview. While some didn't seem too interested in hearing the full explanation others wanted to listen until the end. Each case was dealt with within the guidelines of the university ethical guidelines. Interviewees were presented with the standard consent form (please see Appendix 1-below). Some happily signed the form but others preferred not to, while still agreeing to participate. Another sheet explaining the research topic (please see Appendix IX.2 below) was also shown to all interviewees. Interviewees were informed of their right to decline the invitation to be interviewed and to withdraw from the study at any time they wished to do so, as well as to decline to answer any question. One question was declined by two interviewees, it was the same question, and concerned the number of clients/groups they were managing at the time of interviews. Only two business managers

---

<sup>17</sup> The guidelines can be found in the following web site:  
<http://calendar.waikato.ac.nz/assessment/ethicalConduct.html>

declined to be interviewed. This was because one was on leave during the proposed interview period and the other introduced another interviewee instead.

#### **III.7.4 Pilot interviews**

Pilot interviews are highly advisable and recommended (Kvale, 2007; Saldaña, 2009; Walker, 1985; Weiss, 1994), using interviewees as much like the scheduled interviewees as possible (Maxwell, 2005). A number of reasons have been cited for these recommendations. Clarifying the aims and the frame of the research before starting the actual interviews is one reason. Weiss (1994) adds that “even with pilot interviewing, however, the boundaries of the study’s frame are likely to shift as more is learned [and subsequently incorporated], although as the study proceeds they should shift less and less” (p. 15-16).

Furthermore “quite apart from the issue of its breadth, deciding just what areas the substantive frame should include can be difficult. Not only is it likely that an initial listing of areas of useful information would be incomplete, but there may be several different approaches that could be taken to explanation or description [this is exactly what I found with my use of lending technologies...], each of which would require development of different areas” (Weiss, 1994, p. 16). Pilot interviews help cement and finalise all that, including the study’s aim,

what to include/add into the list of questions, how to ask, etc. That is because pilot interviews/studies would also help in developing “the study’s substantive frame in consultation with members of its primary audience” (p. 16) who are the experts in that area, so as to include all issues of critical importance to the study (i.e. what should be asked). It is also important for deciding/refining the issue of “who should be asked/interviewed”. So pilot interviews would then help in developing what should be asked, who should be asked, and how to ask them.

Regarding the role of pilot interviews in helping the researchers in their task of ‘how to ask’, Maxwell (2005) provided the following explanation. “One important use that pilot studies have in qualitative research is to develop an understanding of the concepts and theories held by the people you are studying—what is often called ‘interpretation’. This is not simply a source of additional concepts for your own theory, ones that are drawn from the language of participants...it provides you with an understanding of the meaning that these phenomena and events have for the people who are involved in them, and the perspectives that inform their actions. These meanings and perspectives are not theoretical abstractions; they are real, as real as people’s behaviour, though not as directly visible” (p. 58).

Pilot interviews, being a small scale study, are designed to test the interview questions in terms of checking the quality of the questions, testing whether they make sense to the interviewees or not, and allowing rewording of the questions in order to improve their quality and efficiency (Easterby-Smith et al., 2002). This is because pilot interviews can reveal deficiencies in the wordings and sequencing of the questions. The objective of pilot interviews is to help in addressing all of those deficiencies before time and resources are expended on the actual interviews.

So, for all those cited reasons and others mentioned in the different interviews literature the proposed interview questions were tested with two pilot interviews. The two pilot interviews were very useful in a number of ways, including the rewording of certain questions, adding some and dropping some, sequencing of some questions, and for making some necessary changes in the initial proposed interviewing approach.

#### **III.7.5 Interview protocol:**

The interviews took place at the interviewees' bank premises (place of work) (apart from three at the suggestion of the interviewees) at an agreed time. The interviews started with general questions such as the interviewees' position in the bank, the kind of businesses s/he deals with and/or the general problems they face when dealing with those

businesses. These initial questions were intended to initiate the discussion, break the ice between interviewer and interviewees, and to probe the general characteristics of the businesses that the relationship managers' interviewees deal with. As mentioned earlier (section III.7-above), the interviews were semi structured with distinct parts; one such part was related to questions about the process of lending. Another concerned the definition of relationship banking for the interviewees and to the banks they are working for. Across all the interviewees, the final section was deliberately reserved for questions about the main topic, the benefits for relationship banking for banks in their dealings with SMEs and how they secure these benefits.

This final section opened with a question around the benefits of relationship banking to the interviewee in dealing with their SME clients and their bank. Interviewees were given sufficient time to enumerate what they perceived the benefits to be and to elaborate on them if they chose. If no elaboration was given, then further questions clarifying the process of securing those benefits were asked after each specific benefit was mentioned or a note was made, and the benefit process was followed up later when deemed appropriate. The approach taken was dependent on the individual interview.



Following the interviewees' enumeration of benefits a further question, designed to stimulate further thinking, was asked:

***Are there any other benefits that you, as a bank manager and/or your bank, think can be attributed to relationship banking (no matter how small)?***

Once this process was exhausted, additional benefits, not specifically mentioned by interviewees, were hinted at to allow interviewees to raise or refute them. Fictitious scenarios were also used here as thought experiments (Lave and March, 1975; Maxwell, 2004) to subtly convey those hints. An example of this was:

***This is a time when you say YES when a loan application is accepted; there is before and there is after. How does relationship banking help before and after and during? I'm assuming here that for example there are three phases; (1) is when a loan application comes in, and (2) assessment and getting all the information, and (3) once it is accepted the price is going to be discussed or decided along with the conditions. At that level how does relationship banking help?***

A final technique was to ask about the benefit using direct questions if/when all other methods were exhausted and some benefits raised in the literature or emerging from and/or through the previous interviews had still not been mentioned by the interviewee. Once the interview themes were exhausted, the researcher asked the interviewee if s/he would like to add anything to her answers or ask any questions of the researcher.

The interviews were recorded<sup>18</sup>, transcribed, and lasted between 41 minutes and 2 hours and 28 minutes with an average of 1 hour and 33 minutes per interview. Interviews were then coded and analysed using the six phases of ‘thematic analysis’ as recommended by Braun and Clarke (2006). This process is dealt with in the next section.

### **III.8 Thematic analysis**

The high volume of raw data produced using a qualitative research method such as interviews (over 350,000 words in the current thesis), can be very interesting to read but it will not elucidate the phenomenon under study until/unless that data is systematically analysed (Bosit, 2003). This data analysis is the most difficult and most crucial aspect of qualitative research (Bosit, 2003), and it has been defined as “the search for patterns in data for ideas that help explain why those patterns are there in the first place” (Saldaña, 2009, p. 8).

Qualitative data analysis has been described as a “process that requires astute questioning, a relentless search for answers, active observation, and accurate recall. It is a process of piecing together data, of making the invisible obvious, of recognising the significant from the insignificant, of linking seemingly unrelated facts logically, of fitting categories one with another, and of attributing consequences to

---

<sup>18</sup> The recorder failed for one interview.

antecedents. It is a process of conjecture & verification, of correction & modification, of suggestion and defence. It is a creative process of organising data so that the analytic scheme will appear obvious” (Morse, 1994, p. 25).

The end result of such data analysis, dubbed as a process of moving from the practical to the general and from the real to the abstract (Saldaña, 2009), is what Tesch (1990) called ‘data condensation’ or ‘data distillation’. The data is not, therefore, simply ‘less’ after the process but ‘sifted’ to highlight pertinent portions from the rest. This is the process of “interpretation and organization” (Basit, 2003, p. 144).

Different data analysis methods exist, however for this thesis, the method of choice was thematic analysis which was undertaken manually and without the assistance of any software (such as NVivo). Thematic analysis has been described as a widely used analysis approach (Braun & Clarke, 2006) although no precise definition of what it is seems to exist (Braun & Clarke, 2006).

Thematic analysis was defined as a search for emergent themes important for description of the phenomenon under study (Daly, Kellehear, & Gliksman, 1997). This process then requires the identification of themes through what Rice and Ezzy (1999) described as a “careful reading and re-reading of the data” (p. 258). It has also

been defined as “a form of pattern recognition within the data, where emerging themes become the categories for analysis” (Fereday & Muir-Cochrane, 2006, p. 82). Elsewhere thematic analysis has simply been defined as “based on the identification of themes in qualitative material, often identified by means of a coding scheme” (<http://people.brunel.ac.uk/~hsstcfs/glos>).

However, Braun and Clarke (2006) seem to have provided a more comprehensive definition, partly from a review of thematic analysis literature, stating that thematic analysis is “a method for identifying, analysing and reporting patterns (themes) within data. It minimally organizes and describes...data set in (rich) detail” (p. 79). Further, making reference to Boyatzis (1998), Braun and Clarke added that often thematic analysis does more than that by also “interpret[ing] various aspects of the research topic” (p. 79).

At this stage, and before any further details related to thematic analysis and how it was used in this thesis are discussed, two things must be highlighted. One, the use of thematic analysis with any epistemological and theoretical framework is reported to be valid (Braun & Clarke, 2006; Malik & Coulson, 2008) such as the realist type of study guiding the current thesis. Two, a key feature of data analysis in qualitative research in general, and thematic analysis in particular, is that it tends to be an on-going and nonlinear procedure

involving an iterative process moving back and forth between the different thematic analysis phases as needed (these phases will be detailed shortly), and indeed making the boundaries between the different phases fuzzy (Braun & Clarke, 2006; Denscombe, 2007), as well as a recursive process that involves continuous movement backward and forward between “the entire data set, the coded extracts of data that [the researcher is] analysing, and the analysis of the data that [s/he is] producing” (Braun & Clarke, 2006, p. 86).

A systematic approach to thematic analysis by reporting the process and detail of the analysis following Braun and Clarke’s (2006) six-point step-by-step guide was followed to analyse the data in the current thesis. The six steps process of thematic analysis is summarised in Table 6 (below) and are detailed next.

**Table 6: Phases of thematic analysis**

<b>Phase</b>	<b>Description of the process</b>
1- Familiarising yourself with your data:	Transcribing data (if necessary), reading and re-reading the data, noting down initial ideas.
2- Generating initial codes:	Coding interesting features of the data in a systematic fashion across the entire data set, collating data relevant to each code.
3- Searching for themes:	Collating codes into potential themes, gathering all data relevant to each potential theme.
4- Reviewing themes:	Checking if the themes work in relation to the coded extracts (Level 1) and the entire data set (Level 2), generating a thematic ‘map’ of the analysis.
5- Defining and naming themes:	On-going analysis to refine the specifics of each theme, and the overall story the analysis tells, generating clear definitions and names for each theme.
6- Producing the report:	The final opportunity for analysis. Selection of vivid, compelling extract examples, final analysis of selected extracts, relating back of the analysis to the research question and literature, producing a scholarly report of the analysis.

Source: Braun and Clarke (2006)

### **III.8.1 The first step**

Entitled “familiarise yourself with your data”, this phase consisted of a careful listening and reading of the professionally transcribed interviews. The purpose of this phase was to familiarise myself with the entire data set in one go, to check the accuracy of the transcripts back against the audio recordings, to review and add the field notes into the transcribed interviews and to record and recall the wide ranging notes of the initial ideas (Braun & Clarke, 2006; Denscombe, 2007; Willig, 2001). This phase was mostly inductive as recommended by Joffe and Yardley (2004) that is to ensure that codes are strongly linked to the data set.

### III.8.2 The second step

If, as noted above, data analysis was described as the most important and crucial part of the qualitative research, then the second phase of thematic analysis, generating initial codes, plays a central role in virtually all qualitative data analysis methods in general but much more so in thematic analysis (Gibbs, 2008). Basit (2003) also identifies the coding step as “one of the significant steps taken during analysis to organize and make sense of textual data” (p. 143). So what is coding?

Coding has been outlined as the partition/subdivision of data and the assignment of categories (Dey, 1993) resulting in codes. “A code in qualitative inquiry is most often a word or short phrase that symbolically assigns a summative, salient, essence-capturing and/or evocative attribute for a portion of language-based or visual data” (Saldaña, 2009, p. 3). Further, a code can descriptively and interpretively grasp an idea that evokes meanings in data (Braun & Clarke, 2006; Saldaña, 2009). For Braun and Clarke (2006), it identifies a semantic content or latent feature of the data appearing to be interesting to the researcher-analyst referring to what Boyatzis (1998) described as “the most basic segment, or element, of the raw data or information that can be assessed in a meaningful way regarding the phenomenon” under study (p. 63). Basit (2003) has

named codes as “tags or labels for allocating units of meaning” (p. 144). These tags are attached to information. They are attached to words or sentences, phrases or paragraphs where they relate (or do not) to a specific setting. According to Miles and Huberman (1994), codes can take many forms such as a direct category label or tag, or a metaphor which is a more complex label.

The start of the second phase is recommended to consist of generating initial codes, tagged free or open codes from the initial notes as well as in response to items of interest within the data (Braun & Clarke, 2006). Table 7 (below) provides an example of a data extract from an interview and two initial codes applied to it.



**Table 7: An example of data extract with two initial codes**

Data extract from interview 9	Codes
Not actually getting; I suppose they <sup>19</sup> re reliant on an external accountant to provide the information. So the accountant's got to provide information but the accountant is often sort of saying "Well I need the client to actually provide me some information before I can prepare some financial management accounts for you," so yeah a lot of these people just don't have; if we want to see a debtor and creditor age listing a lot of those people can't do it. And they are reluctant to pay the money for an accountant to do it if it's on an interim basis. I mean often they will say "Look, we'll get your accountant to provide information at the end of the year but we don't want to have to pay for an accountant to come and provide information on a quarterly or six monthly basis." So there is a reluctance to spend money on an accountant.	<p>1- Small businesses rely on external accountants to provide financial management accounts (e.g. debtor &amp; creditor age listing).</p> <p>2- Reluctance of SME owners to ...Lot of small business owners reluctant to pay money especially more than once a year.</p>

### *III.8.2.1 Coding guidelines and criteria*

Different criteria and strategies exist for identifying codes. Some of the criteria include the identification of recurring meanings even when different words are used. Another criterion is repeated and consistent patterns of actions described as forceful discourses (Bazeley, 2007; Owen, 1984; Saldaña, 2009). A strategy associated with coding data, that were used in this thesis, include inductive and a priori coding, also referred to as data-driven and theory-driven, respectively (Braun & Clarke, 2006). In the former, the codes identified are/were dependent on the data, as was the case in Table 7 (above), and those

---

<sup>19</sup> i.e. small businesses

emerging codes were generated by the thesis's author from examining the data directly and solely. An example was the relationship banking benefit dubbed 'humanisation of the bank' (please see section VI.6-below for more details). However in the latter case, data is approached with specific questions in the researcher's mind such as those around - in the context of the current thesis - the process of securing a specific relationship banking benefit (e.g. cross selling), what type of information would allow a relationship bank manager to do that, how does s/he obtain that information, and how would s/he use this information. Thus the analysis here was guided by specific themes which are related to the thesis's aim and research questions that were developed before data collection.

A number of advices and guidelines have been detailed in the literature regarding how to conduct successful coding (Bosit, 2003; Bogdan & Biklen, 1992; Braun & Clarke, 2006; Flick, 2002; Foss & Waters, 2003; Saldaña, 2009; Taylor & Gibbs, 2010; Welsh, 2002). For example, Braun and Clarke (2006) emphasised that "it is important in this phase [i.e. coding] to ensure that all actual data extracts are coded, and then collated together within each code..., [and] remember that you can code individual extracts of data in as many different 'themes' as they fit into - so an extract may be uncoded, coded once, or coded many times, as relevant" (p. 89). With

regard to the task of choosing the most appropriate coding methods, Flick (2002) offers a checklist of general criteria to help with that. These criteria include the advice that the coding method(s) should relate to addressing the project's research questions. The coding method of choice should also lead the researcher toward an analytic pathway constructing categories and taxonomies and developing patterns and themes. The guidelines and attendant advice has been followed as much as possible.

#### *III.8.2.2 Coding methods*

Different coding methods exist and many categorisation of these coding methods have been suggested (Saldaña, 2009). Several coding methods can be used to analyse the same data in one study. One such categorisation is that of Saldaña (2009) who classified coding methods into first cycle methods and second cycle methods. The first coding methods have been referred to as simple, direct, and mostly employed in the initial stages of data analysis. Well over thirty first cycle methods or techniques of coding exist, some of which are structural, hypothesis, procedural and process coding methods (Saldaña, 2009). The second cycle methods, more than five, have been described as “more challenging because they require such skills as classifying, prioritising, integrating, synthesising, abstracting, conceptualising, and theory building” (Saldaña, 2009, p. 45). Further and when required,

the key role from using these second cycle methods is to develop, from the range of codes developed during the first cycle of coding, an organising map of categories, themes, concepts, and theory. In other words, the first cycle codes along with their associated data transcripts are refined and rearranged to analyse at a deeper and more abstract level with the aim of producing a list of a lesser number, broader in meaning or more encompassing as the researcher moves from codes to categories, themes and concepts (Lewins & Silver, 2007; Saldaña, 2009). This is because, as (Saldaña, 2009) neatly puts it, "before categories are assembled, your data have to be recoded because more accurate words or phrases were discovered for the original codes; some codes will be merged together because they are conceptually similar; infrequent codes will be assessed for their utility in the overall coding scheme; and some codes that seemed like good ideas during first cycle coding may be dropped all together because they are later deemed "marginal" or "redundant" after the data corpus has been fully reviewed" (p. 149).

The current study used several coding techniques and this was dictated by the study's conceptual framework/paradigm, the purpose of the study being to uncover the processes of how banks secure relationship banking benefits, and to enable the analysis that would help directly answering the research questions (Saldaña, 2009). However, the

profile of three coding methods only (two from the first cycle methods of coding –namely the structural and the process coding methods- and one from the second cycle methods –the pattern coding method<sup>20</sup>-), will be outlined including a short description of each method and its function, its general purpose and projected outcome, and how it is appropriate/relevant to the current thesis.

#### III.8.2.2.1 The structural coding method

To specifically help with addressing the research questions (Flick, 2002) a coding method of choice was the structural method of coding which is intended to assist with organising the data corpus around the thesis's research questions (Saldaña, 2009). This method has been defined as a question-based code (MacQueen, McLellan-Lemal, Bartholow, & Milstein, 2008) that "acts as a labelling and indexing device, allowing researchers to quickly access data likely to be relevant to particular analysis from a larger data set" (Namey, Guest, Thairu, & Johnson, 2008, p. 141). Saldaña (2009) further described structural coding as a method that uses a "content-based or conceptual phrase representing a topic of inquiry to a segment of data -that relates to specific research question used to frame the interview" (2009, p. 66). This is to both code and categorise the data corpus. Hence, MacQueen et al. (2008) and Namey et al. (2008) suggest structural

---

<sup>20</sup> However, because Pattern coding method was used as part of the third step of thematic analysis, its profile is discussed in the third step of thematic analysis.

coding is more suitable for interview transcripts, which is the data in current thesis.

The objective is to make the next step of the analysis easier “by identifying all of the text associated with a particular question and associated probes” (MacQueen et al., 2008, p. 124) with the resulting structural codes (such as benefits of relationship banking that the banks’ relationship managers enumerated during the interviews) constituting the foundation work for further detailed coding and analysis. The similarly coded segments are then collected together for more detailed coding (Saldaña, 2009). For example, using the enumerated relationship banking benefits, the taxonomy and pattern coding methods of Saldaña (2009) to construct a ‘taxonomy of relationship banking benefits accruing to bank’ including some specific criteria of inclusion/exclusion or by adding a new cell into the taxonomy. MacQueen et al. (2008) put it this way; "structural coding generally results in the identification of large segments of text on broad topics; these segments can then form the basis for an in-depth analysis within or across topics” (p. 125). Methods that are recommended (Corbin & Strauss, 2008, pp. 96-97) for further analysis of the resulting codes, relevant to the thesis, were thematic analysis and within-case and cross-case displays.

#### III.8.2.2.2 The process coding method

Process coding, which often employs gerunds to denote action in the data (Charmaz, 2002) such as ‘asking for information’, ‘assessing information’, and ‘accessing information’, is another coding method that was used to analyse the data. This coding method has been particularly recommended for studies that search for processes defined as "on-going action/interaction...taken in response to situations, or problems, often with the purpose of reaching a goal or handling a problem...[These processes] occur over time, involve sequences of different activities and interactions...responses (though not always obvious), and have a sense of purpose and continuity" (Strauss & Corbin, 1998, p. 169). A goal/problem for relationship banking managers is often to do with seeking, accessing, and evaluating information about small business owner/managers and their businesses. Sub-processes, however, are "the individual tactics, strategies, and routine actions that make up the larger act" (Strauss & Corbin, 1998, p. 169) that the banks’ relationship managers would follow and do in order to reach their goals and/or solve their problems.

When writing about the coded data (using process coding), as part of doing analysis, Saldaña (2009) recommends the use of story-line conventions such as the first step, the second step, and the turning point. Saldaña (2009) further added that “participant language with

transitional indicators such as, ‘if’, ‘when’, ‘because’, ‘then’, and ‘so’, etc., clue the researcher to a sequence or process in action. These sequences or processes can be ordered as a numeric series of actions, listed as a bullet-pointed set of outcomes, or graphically represented with first-draft illustrations as a flow diagram” (p.79). An example (Table 8 - below) using the data extract from interview 9 (Table 7 - above) shows an instance of a process in action which then was presented in a series of actions during the analysis process.

**Table 8: an example of a process in action**

Data extract from interview 9	
Not actually getting; I suppose they're reliant on an external accountant to provide the information. So the accountant's got to provide information but the accountant is often sort of saying "Well I need the client to actually provide me some information before I can prepare some financial management accounts for you," so yeah a lot of these people just don't have; if we want to see a debtor and creditor age listing a lot of those people can't do it. And they are reluctant to pay the money for an accountant to do it if it's on an interim basis. I mean often they will say "Look, we'll get your accountant to provide information at the end of the year but we don't want to have to pay for an accountant to come and provide information on a quarterly or six monthly basis." So there is a reluctance to spend money on an accountant.	<p>When a relationship manager needs a debtor and creditor age listing  Because small businesses are reliant on external accountants to provide information to their relationship managers such as debtor and creditor age listing  <b>First</b> small businesses have to provide their external accountant with the necessary information  <b>Second</b>, the accountant will use the provided information to prepare the financial management accounts (debtor and creditor age listing in this case)  <b>Third</b>, the debtor and creditor age listing will be given to the relationship manager  <b>Forth</b>, the relationship manager will assess the listing  <b>Fifth</b>...</p>

Process coding was particularly helpful and was used extensively to investigate and identify the processes of how banks/relationship



managers secure relationship banking benefits for the benefits of their banks.

The many process codes produced during this stage are then condensed by way of the researcher's reflection using analytic memo writing and second cycle method(s) of coding (Saldaña, 2009). This is how further analysis is performed during which Dey (1993) recommends that the researcher considers the complex interplay of the many factors that make up a process and how s/he "obtain[s] a sense of how events originate and evolve, and their shifting significance for those involved. Process refers to movement and change over time. In place of a static description, [s/he] can develop a more dynamic account of events" (Dey, 1993, p. 39).

### **III.8.3 The third step**

An outcome from phase two was a lengthy list of codes. The third phase re-focuses the analysis at a higher and wider level moving from codes to themes. In essence, the goal then is to begin with the analysis of the codes produced and ponder how those codes might be combined towards making overarching themes (Braun & Clarke, 2006). Braun and Clarke (2006) suggested using tables or mind maps or even writing the code with a description on a piece of paper and playing around with them. That is exactly the process followed by the researcher here.

### *III.8.3.1 Pattern coding*

At this stage, pattern coding was used as an analytical tool. Saldaña (2009) labelled this as a second cycle coding method. According to Miles and Huberman (1994), pattern codes are "explanatory or inferential codes, ones that identify an emergent theme, and configuration or explanation. They pull together a lot of material into a more meaningful and parsimonious unit of analysis. They are a sort of meta-code" (p. 69). From an organisational perspective, pattern coding is to a qualitative researcher what cluster analysis and factor analysis are in statistical or quantitative analysis (Miles & Huberman, 1994). However, pattern codes contribute to the further analysis process not only by organising the corpus of data but also, and at the same time, via attributing meaning to that organisation (Saldaña, 2009). Miles and Huberman (1994) expressed this idea this way "[pattern coding] helps the researcher elaborate a cognitive map, an evolving, more integrated schema for understanding local incidents and interactions" (p. 69). Moreover, in the case of multi-case studies, by unearthing common themes and processes across cases, pattern coding puts down the foundation(s) meant for cross-case analysis (Miles & Huberman, 1994)

Overall then, pattern coding has been suggested as an appropriate method of coding the data for developing key themes, searching for

rules, causes, and explanations, and developing theoretical constructs and processes” (Daley, 2004; Saldaña, 2009).

Saldaña provided a systematic way of doing pattern coding stating “for second cycle pattern coding, collect similarly coded passages from the data corpus... . Review the first code cycle codes to assess their commonality and assign them a pattern code. Use the pattern code as a stimulus to develop a statement that describes a major theme, a pattern of action, a network of relationships, or theoretical construct from the data” (2009, p. 154). In the current thesis, pattern coding contributed towards not only the construction of the banks benefits taxonomy as presented in Matrix 1 (below p.285), but also with the development, conceptualisation and use of relationship banking both as marketing tool/mechanism and assessment tool/mechanism.

### *III.8.3.2 Searching for themes*

Pattern coding is, and was, a key analytical tool throughout the third phase during which the focus is on moving from coding to theming the data and, from a macro-perspective, on thinking about the emerging/emergent different relationships between codes, categories, and themes. Braun and Clarke explained briefly (another facet of) the process of moving from codes to themes stating “some initial codes may go on to form main themes, whereas others may form sub-

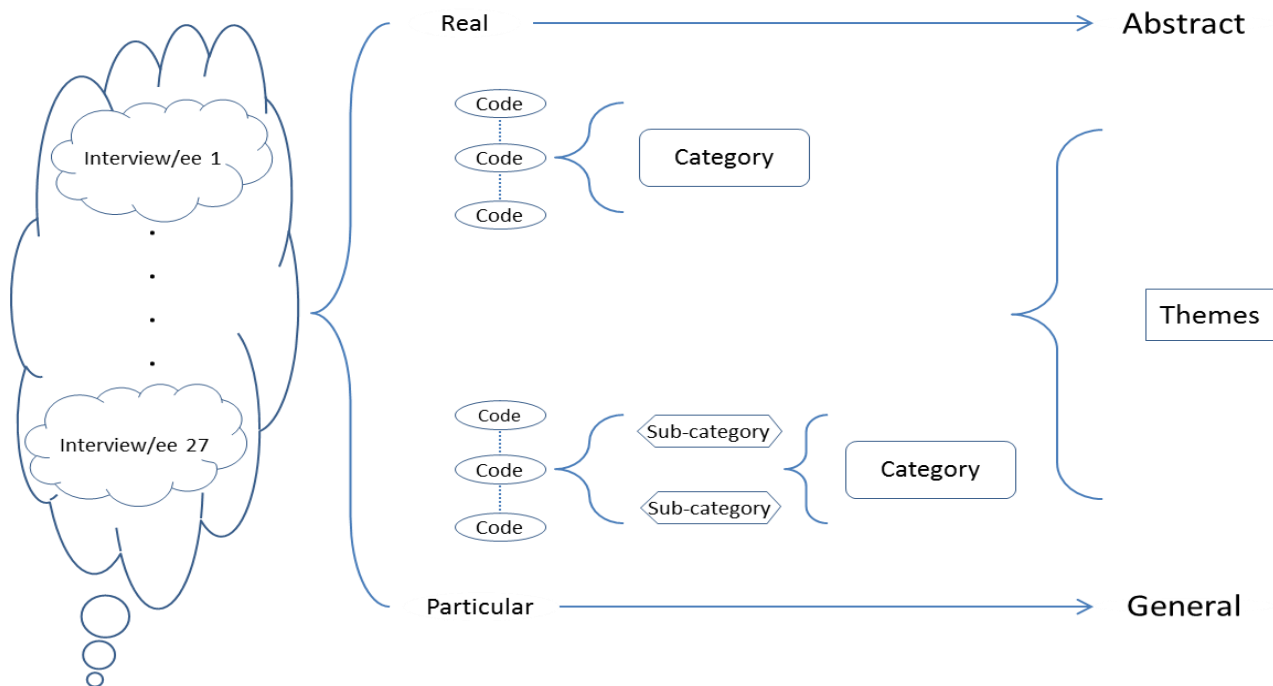
themes<sup>21</sup>, and others still may be discarded. At this stage, you may also have a set of codes that do not seem to belong anywhere, and it is perfectly acceptable to create a ‘theme’ called ‘miscellaneous’ to house the codes - possibly temporarily - that do not seem to fit into your main themes” (2006, p. 90). A theme has been defined as an “outcome of coding, categorization, and analytic reflection” (Saldaña, 2009, p. 13). Further, Rossman and Rallis (2003), explained the difference between a category and a theme inviting researchers to “think of a category as a word or phrase describing some segment of [our] data that is explicit, whereas a theme is a phrase or sentence describing more subtle and tacit processes” (p. 82). Concerning subcategories, Saldaña (2009) explained that “some categories may contain clusters of coded data that merit further refinement into subcategories” (p. 11).

The thematic analysis process of moving from the data corpus (interviews) to codes to categories, and then to themes as well as the different relationships between the resulting codes, categories and themes are illustrated in Figure 3 below.

---

<sup>21</sup> Most qualitative research literature seems to use the concept of categories instead of sub-themes and, from the perspective of, and in the context of this thesis there is no difference between the two hence they are used interchangeably.

Figure 3: A streamlined process of thematic analysis using Saldaña's 2009 model



The streamlined process shows how thematic analysis is undertaken, facilitating and guiding:

1. Moving from the particular to the general by way of “inferring transfer” – inferring that what was identified through the 27 cases studied may possibly also be detected in other comparable relationship banking settings (Saldaña, 2009). The streamlined process also shows how thematic analysis “progresses from the particular to the general by predicting patterns of what may be observed and what may happen in similar present and future contexts” (Saldaña, 2009, p. 13), and
2. Moving from real to abstract: this process begins “when the major categories are compared with each other and consolidated

in various ways”, thus transcending the reality aspect of the data progressing to themes and concepts i.e. more abstract constructs. Richards and Morse (2007) put it this way; “categorizing is how we get ‘up’ from the diversity of data to the shapes of the data, the sorts of things represented. Concepts are how we get up to more general, higher-level, and more abstract constructs” (p. 157) .

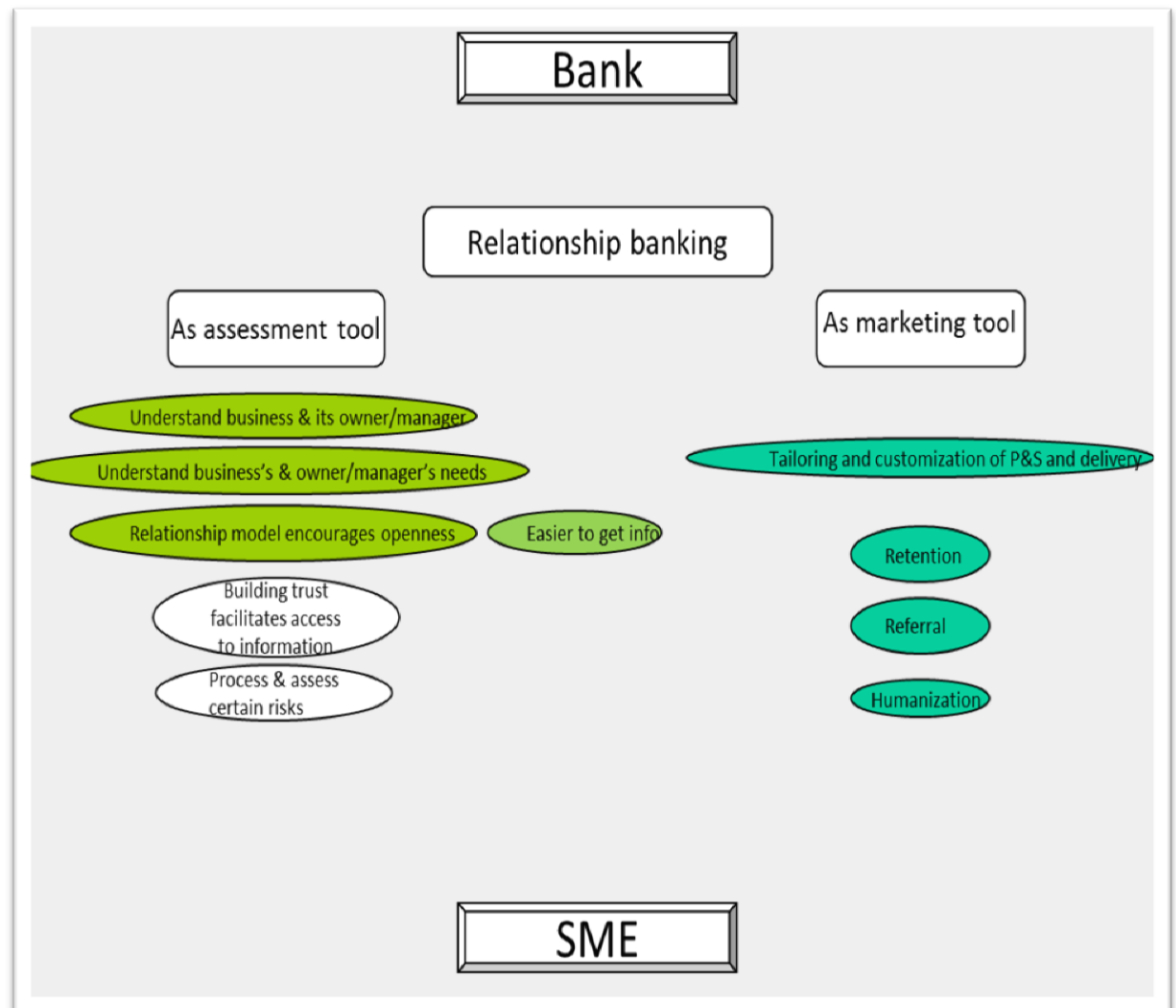
#### **III.8.4 The fourth step**

Phases one through to three resulted in a set of candidate codes, categories, and themes, as well as all of the data excerpts which were coded in relation to them. Phase four starts with reviewing the themes to refine them (Braun & Clarke, 2006). The review is done at two levels. The first is to check the coherence of each theme from within by revisiting and reading all the coded data extracts associated with it. Once that is done, the level two review involves checking the coherence across each and all themes in relation to all the data corpus, “generating a thematic map of the analysis” (Braun & Clarke, 2006, p. 87), and making sure that the generated “candidate thematic map ‘accurately’ reflects the meanings evident in the data set as a whole” (Braun & Clarke, 2006, p. 91). Briefly, a thematic map is generally defined as a schematic representation of a set of themes showing the hierarchical relationship between the themes, their categories and

codes (Braun & Clarke, 2006; Daley, 2004; Novak & Gowin, 1984).

An example of an early stage thematic map from the current study showing some themes, categories, and codes can be seen in Figure 4 below.

Figure 4: an early stage thematic map showing some themes, categories, & codes



Overall, the review process resulted in adding some themes, collapsing few other themes into each other while some of the rest were broken down into separate themes.

### **III.8.5 The fifth step**

Once a comprehensive and satisfactory thematic map was reached, thematic analysis progressed into the fifth phase. In this phase, the task was to clearly define each theme by way of identifying its essence, and giving it a name such as (relationship banking as a tool/mechanism for) “humanising the bank”. Finally, for each individual theme a detailed analysis was written. Here the advice from Braun and Clarke (2006) was that “as well as identifying the ‘story’ that each theme tells, it is important to consider how it fits into the broader overall ‘story’ that [the researcher is] telling about [his or her] data, in relation to the research question or questions, to ensure there is not too much overlap between themes” (p. 91-92).

### **III.8.6 The sixth and final step**

The final phase, being the last opportunity for any further analysis, consisted of producing the report of the analysis, relating it back to the thesis’s aim, research questions and literature. Each of the different constructs (codes, categories, and themes) was discussed showing how they integrate and or relate to each other (Saldaña, 2009). The general advice here was to strive for providing a “concise, coherent, logical, non-repetitive and interesting account of the story the data told - within and across themes.... [Furthermore, the thesis] needs to do more than just provide data. Extracts need to be embedded within an



analytic narrative that compellingly illustrates the story [the researchers is] telling about [his/her] data, and [his/her] analytic narrative needs to go beyond description of the data, and make an argument in relation to [his/her] research question[s]” (Braun & Clarke, 2006, p. 93).

## **Conclusion**

This chapter has discussed the different aspects of the research approach used to investigate the research aim and questions of the thesis. The thesis now turns its attention to the empirical context of banks and SMEs in New Zealand.

## **IV. Empirical context of the study:**

### **banks & SMEs in New Zealand**

#### **Introduction:**

Context is important, as detailed in the section III.5 (above). The context for this thesis is New Zealand; consequently, this chapter is divided into two parts, the first part deals with banking in New Zealand, and the second, SMEs in New Zealand.

#### **IV.1 Banking in New Zealand:**

##### **IV.1.1 A historical overview of the New Zealand financial/banking system.**

Since the 1840s and with the arrival of European settlers, banks have been facilitating the financial requirements of people in New Zealand (New Zealand Bankers' Association, 1997). Also, like the rest of the financial system and the whole economy in general, the New Zealand banking system, from its start, has been shaped by legislation. For example, for a trading bank to be established, a special Act of parliament was required (Grimes, 1998; New Zealand Bankers' Association, 1997).

While over the years successive legislation must have helped establish a good banking system, at a certain point it was realised that at least some of that legislation had become a burden not only on the banking sector but to the whole economy. With regard to this issue, Grimes

(1998) notes that the government regulations and other interventions, which he qualified as pervasive, treated the different market sub-sectors in different ways causing microeconomic distortionary effects as well as macroeconomic efficiency problems. The pre-1984 legislation restricted competition within the finance sector and split the financial services providers into three distinct groups (Grimes, 1998), trading banks, saving banks, and other non-bank financial institutions, thus controlling who operates in each market segment (New Zealand Bankers' Association, 2006).

However, with the rapid development of financial markets in the early 1980s the categories for financial institutions outlined in the legislation became noticeably outdated (New Zealand Bankers' Association, 2006) thus making the 1984-87 deregulation of the finance industry unavoidable (Evans, Grimes, & Wilkinson, 1996). Subsequently, the New Zealand economy in general, and the financial system in particular, underwent substantial reforms and indeed these “transformed it from one of the most regulated of the developed economies to one of the least regulated” (McMillan, 1998, p. 827). The major effect of the deregulation process resulted in removing both the legislation that was behind the restriction of competition and the regulations that controlled who can operate in what financial sector

(New Zealand Bankers' Association, 2006; Reserve Bank of New Zealand, 1986).

The structural changes of the banking industry were legislated by the Reserve Bank of New Zealand Amendment Act 1986 opening up the doors for new banks to enter the market and stipulating that the 'registered bank' would be the only type of 'bank' in New Zealand (Minh To & Tripe, 2002). Thus and ever since, 'registered banks' and 'non-bank financial institutions' have been the only two types of financial institution in New Zealand and apart from the fact that registered banks are the only institutions to use the word bank in their names, non-bank financial institutions are mostly permitted to compete on a par with registered banks (New Zealand Bankers' Association, 2006).

The other changes brought by the post-1984 era included the ability for any registered bank to engage in retail banking, wholesale banking or full service banking. There were no longer artificial limits on the number of banks, nor discrimination between domestic and foreign-owned institutions (Hess, 2008). The number of registered banks in New Zealand thus increased significantly due to a number of foreign-owned non-bank financial institutions, domestic savings institutions and building societies converting to banks as well as the entry of new foreign banks (Tripe, 2004).

Foreign ownership of banks in New Zealand has always been a significant characteristic with “the first bank to open for business in New Zealand, in 1840, [being] a branch of the Union Bank of Australia [which] was a British overseas bank, headquartered in London” (Tripe, 2009, p. 3). However, as a result of deregulation and the free entry of foreign banks, the intensification of the foreign ownership process of banks led into the unrivalled high degree of foreign ownership (as far as developed economies were concerned), thus making this a distinguishing characteristic of the New Zealand banking system (Tripe, 2004).

The degree of foreign ownership increased steadily with assistance from the absorption of the New Zealand-owned financial institutions by foreign banks mergers and acquisitions. Consequently, in the mid-1980's when deregulation occurred, three of the four trading banks were foreign-owned, two by Australian interests and one by British. There was also a significant savings bank sector that was predominantly New Zealand-owned, with exceptions being the so-called private savings banks (which were owned by the trading banks).

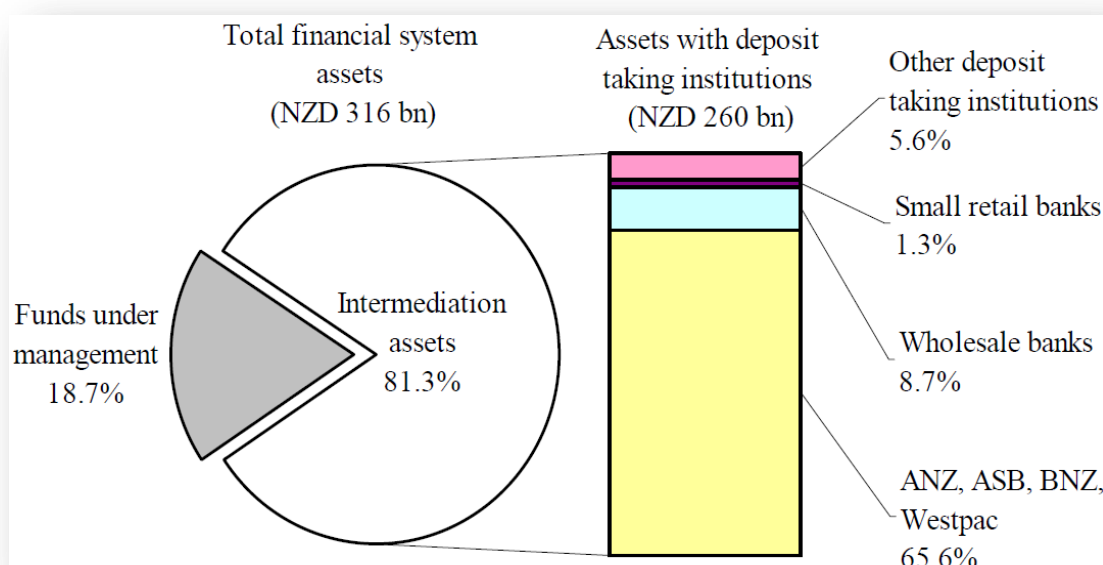
Additionally, there were a number of other New Zealand-owned financial institutions, such as building societies, finance companies and the Rural Bank which was government-owned. However, around

99% of the banking sector assets were under foreign ownership when Westpac Corporation acquired Trust Bank New Zealand (Tripe, 2004), though by the end of June, 2003, the almost 100% foreign ownership banks' assets had decreased to between 85.1% and 90%. It went up to 96.1% by December, 2008 reflecting some of the expansion of the New Zealand owned banking sector particularly through the establishment of Kiwi bank through New Zealand Post by the government (Tripe, 2009).

#### **IV.1.2 Recent developments of the banking system**

Recently, overall, the development of the financial system has been described as patchy with a banking system qualified as sound, large and efficient which exists alongside “equity, venture capital and debt markets that in size, depth, liquidity and skill base are relatively under-developed” (Cameron, Chapple, Davis, Kousis, & Lewis, 2007, p. 19). Consequently, the central position that the banking sector occupies within the financial system, and the central role that it plays in the New Zealand economy can be clearly seen, for example, through Figure 5 (below) with the big four banks, dubbed “systematic banks” by the Reserve Bank of New Zealand (2005), holding 65% of the total assets of the financial system and 85% of the total assets of the banking system. This last figure has risen to nearly 88% during 2012 (KPMG, 2013).

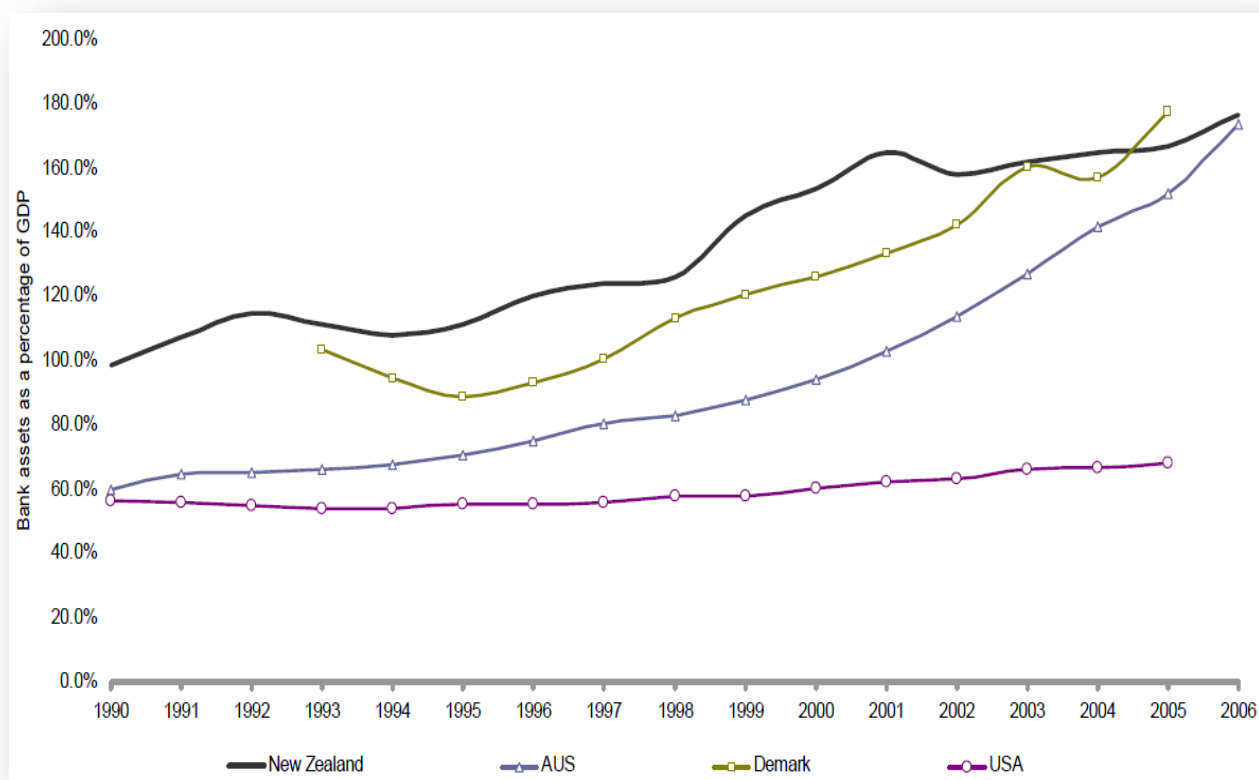
**Figure 5: New Zealand break-down of financial system assets (2004)**



Source: Hess (2008)

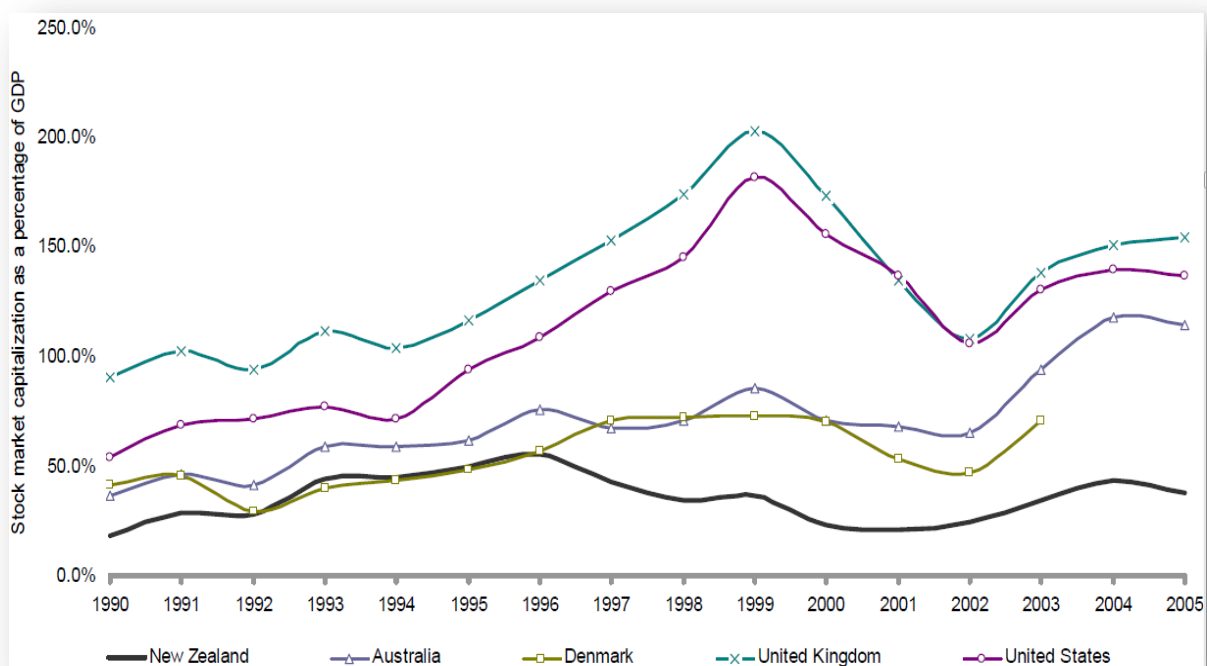
The relative dominance of the banking sector in the New Zealand financial system is also illustrated in Figure 6, and Figure 7. From these figures it is clearly illustrated that business financing in New Zealand has been intermediated mostly by banks and that, as Figure 8 (below) shows they are still considered to be the principal supplier of business lending (KPMG, 2013; Statistics New Zealand, 2004).

**Figure 6: Size of banking sector: selected countries**



Source: Cameron et al. (2007)

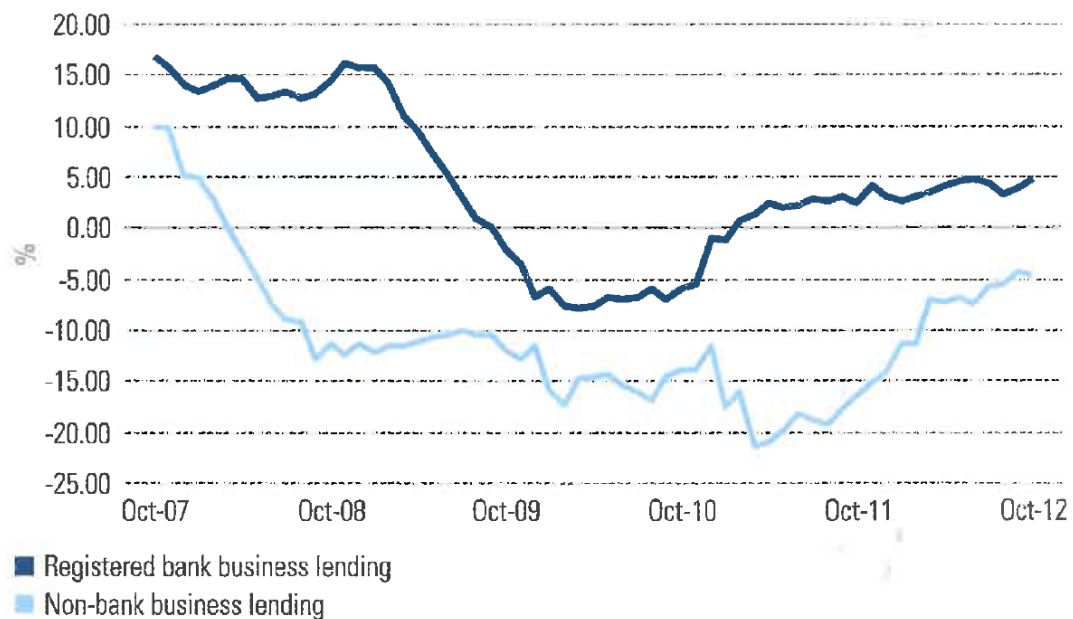
**Figure 7: Stock market capitalisation: selected countries**



Source: Cameron et al. (2007)



**Figure 8: Increase in registered bank and non-bank business lending**



Source: (KPMG, 2013)

The 1980's structural reforms of the banking industry have been hailed by some critics as giving "New Zealand one of the most competitive, flexible and service-oriented banking industries in the world" (New Zealand Bankers' Association, 2006, p. 8). However, some studies (Chan, Schumacher, & Tripe, 2007; Matthews, 2009; Smith & Tripe, 2001; Tripe, 2007) have raised the issue of possible monopolistic competition in the banking sector. For example, Smith and Tripe (2001) found that for the period 1996-1999 "total bank revenues appeared to be earned under monopolistic competition" (p.13). A similar and more recent study by Chan et al. (2007) examining the banking market over the longer period of 1996-2005 came to the same conclusion as Smith and Tripe (2001).

A counter criticism, however, is based on the small size of the economy, and at least from the New Zealand Bankers' Association (2006) point of view, to remain profitable, the margin squeezes resulting from the competitive pressures have made the continuous restructuring of banks in New Zealand necessary. This is beside the fact that no restrictions on the entry of new banks exist. Furthermore, “over-capacity in the supply of financial services has been a constant theme and one given credence over the last 20 years by the mergers of ANZ and Postbank, United Bank and Countrywide Bank, the Rural Bank and the National Bank (of New Zealand), National Australia Bank’s purchase of the Bank of New Zealand, Westpac Banking Corporation’s purchase of Trust Bank New Zealand, the National Bank’s purchase of Countrywide Bank, and most recently, the ANZ’s purchase of the National Bank” (New Zealand Bankers' Association, 2006, p. 9). Figure 9 (below) shows the series of mergers and acquisitions that occurred over the years leading to the existence of four systematic banks as of 2004.

**Figure 9: Genealogy of New Zealand banks**

	Auckland Savings Bank	ANZ	National Bank	Rural Bank	Countdown Building Society	Bank of New Zealand	Bank of New South Wales	Commercial Bank of Australia	Regional Savings & Trust Banks	
1979		NZ Subsidiary formed				state-owned since 1945				1979
1980		25% of shares placed with investors								1980
1981										1981
1982							Merger forms Westpac			1982
1983										1983
1984										1984
1985		shares repurchased by parent 1986								1985
1986										1986
1987						Govt sells 25% of shares				1987
1988	>ASB corporized,			registered	Registration and name change				Trust Bk Group formed	1988
1989	>CBA majority	acquires Post Bank								1989
1990	acquires Westland Bk			sold to Fletcher Group						1990
1991										1991
1992			acq. Rural Bank	← Rural Bank	acquires United Bank					1992
1993				Bank	RBSC full control bought by NAB					1993
1994	amalgamates Post Bank								amalgamation of members	1994
1995										1995
1996							acquires Trust Bank	← --- Trust Bank		1996
1997										1997
1998			acquires Countrywide	← --- Countdown Bank						1998
1999										1999
2000	CBA takes full control									2000
2001										2001
2002			NBNZ							2002
2003	↓	acquires NBNZ	← ---			↓		↓		2003
2004	ASB	ANZ				BNZ		Westpac		2004

Source: Hess (2008, p. 99)

As at 28 February, 2012, there were 21 banks registered with the Reserve Bank and operating in the New Zealand market (Table 9-below).

**Table 9: Registered banks in New Zealand as of 28 February 2012**

<b>Name of registered bank</b>	<b>Registration Date</b>
ANZ National Bank Limited	1 April 1987
ASB Bank Limited	11 May 1989
Australia and New Zealand Banking Group Limited (B)	5 January 2009
Bank of Baroda (New Zealand) Limited	1 September 2009
Bank of India (New Zealand) Limited	31 March 2011
Bank of New Zealand	1 April 1987
Citibank N A (B)	22 July 1987
Commonwealth Bank of Australia (B)	23 June 2000
Deutsche Bank A G (B)	8 November 1996
JPMorgan Chase Bank NA (B)	1 October 2007
Kiwibank Limited	29 November 2001
Kookmin Bank (B)	14 July 1997
Rabobank Nederland (B)	1 April 1996
Rabobank New Zealand Limited	7 July 1999
Southland Building Society	7 October 2008
The Bank of Tokyo-Mitsubishi UFJ(B)	1 March 2004
The Co-operative Bank Limited	26 October 2011
The Hongkong and Shanghai Banking Corporation (B)	22 July 1987
TSB Bank Limited	8 June 1989
Westpac Banking Corporation (B)	1 April 1987
Westpac New Zealand Limited	31 October 2006

**Note:** Banks marked (B) operate in New Zealand as branches of overseas-incorporated banks. All other banks are incorporated in New Zealand.

**Source:** Reserve Bank of New Zealand (2012)

The New Zealand banking scene is predominantly a branch banking structure dominated by five major bank brands out of the 21 registered banks in New Zealand (Reserve Bank of New Zealand, 2012). The five major bank brands, being ANZ, ASB, BNZ, National and Westpac, are all Australian-owned. Together these banks represent 87.76% of the total assets of with the whole banking sector in New Zealand (KPMG, 2013), and about two thirds of banks' business loans

are made to small businesses in New Zealand (Ministry of Economic Development, 2003a). While there are some other foreign and local banks operating (as per Table 9-above) in the New Zealand market, these either do not transact with business clients, are so small as not to register in terms of the percentage of lending, are not present everywhere and/or are not branch driven. These minor banks are not included in the analysis.

It is also important to note that in New Zealand there is little transparency in terms of bank charges (Boulanouar & Locke, 2009) and proximity of a bank office seems to be an important variable in the choice of which bank small businesses will use (Locke & Drever, 2008).

#### **IV.1.3 Focal Banks & relationship banking**

The focus of this study is on the banks dealing with SMEs in New Zealand. The five bank brands mentioned above, have been identified as being actively involved with the SME sector, each with an extensive branch network throughout the country and together total 840 (842) branches out of all the total registered banks branches of 1236 (1243) in 2012 (2011) (KPMG, 2013).

Other measures of size and strength, as well as profit measures for these focal banks is clearly shown in Table10 , (below), in a

comparative fashion with some of the other registered banks, as well as the whole banking sector.

: Comparative size and performance measures of the focal banks 10 Table

	Balance date	year	Rank by total assets	Total assets \$Million	ROE %	ROA %
Australia and New Zealand Banking Group Limited-New Zealand Banking (ANZ) Group	30-Sep	2012	1	127,467	14.34	0.99
	30-Sep	2011		128,089	13.32	0.86
Bank of Baroda (New Zealand) Limited	31-Mar	2012	16	61	1.71	1.22
	31-MAr	2011		53	0.48	0.42
Bank of India (New Zealand) Limited	31-Mar	2012	17	55	0.04	0.04
	31-MAr	2011		50	0.00	0.00
Bank of New Zealand (BNZ)	30-Sep	2012	3	72,945	12.05	0.79
	30-Sep	2011		73,933	16.07	0.93
Commonwealth Bank of Australia New Zealand Banking Group	30-Jun	2012	4	69,192	16.50	1.04
	30-Jun	2011		68,351	15.00	0.87
Kiwibank Limited	30-Jun	2012	5	14,745	11.66	0.55
	30-Jun	2011		13,873	3.55	0.16
Rabobank Nederland New Zealand Banking Group	31-Dec	2012	6	10,495	11.31	0.87
	31-Dec	2011		9,449	15.96	0.92
TSB Bank Limited	31-Mar	2012	7	5,165	12.69	0.96
	31-Mar	2011		4,850	11.56	0.86
Westpac Banking Corporation	30-Sep	2012	2	77,329	14.77	0.98
	30-Sep	2011		77,768	14.98	0.89
Bank sector total		2012		395,918	14.30	0.93
		2011		394,613	14.10	0.84

Source: (KPMG, 2013)

The facilities offered to SME customers have traditionally been broadly comparable across the banks (Boulanouar & Locke, 2009; Ministry of Economic Development, 2003a), although new products are emerging.

A detailed study by PricewaterhouseCoopers, commissioned by the Ministry of Economic Development, focussed on bank lending practices to small and medium sized enterprises (SMEs) (Ministry of Economic Development, 2003a), surveying the five bank brands plus Hong Kong and Shanghai Banking Corporation (HSBC) & TSB Bank Limited. The report concluded that “all of the banks regard the SME sector as an important part of their portfolio. They perceive growth opportunities and consider the market for this sector to be competitive” (Ministry of Economic Development, 2003a, p. 1).

With regard to the focus of this study/thesis - relationship management - the report also highlighted that:

- Many of the banks in the New Zealand market are targeting the SME sector. A number of tools are being used to increase the banks’ focus on the sector, and these include undertaking and publishing market research, a shift toward more emphasis on relationship management and greater use of performance measures at relationship manager level aimed at growing the SME loan book.
- Many of the banks perceive the SME sector to be profitable and so are deploying more resources to capture greater market share. To facilitate this, banking services are being packaged

differently into a combined service, offering more economic and business related information to their SME customers and renewed emphasis on relationship management.

- Furthermore, banks are also defending existing client relationships. This means undertaking more regular reviews of facilities and pricing reductions to match competitive offers.

Historically, banks in New Zealand have not been assigning a business or relationship manager to every business that has a business account with them (Ministry of Economic Development, 2003a). These managers are assigned to SME customers only when they reach a certain size based on turnover, complexity of the business, and/or on facilities contracted (Ministry of Economic Development, 2003a). Only those banks staff involved in relationship banking were targeted for this study/thesis.

Reflecting the increasing interest in this sector by banks was outlined in the PricewaterhouseCoopers report as evidence that banks were beginning (as at 2003) to bring back more of a relationship approach to the SME market, and to place more resources at the customer interface level. Specifically:

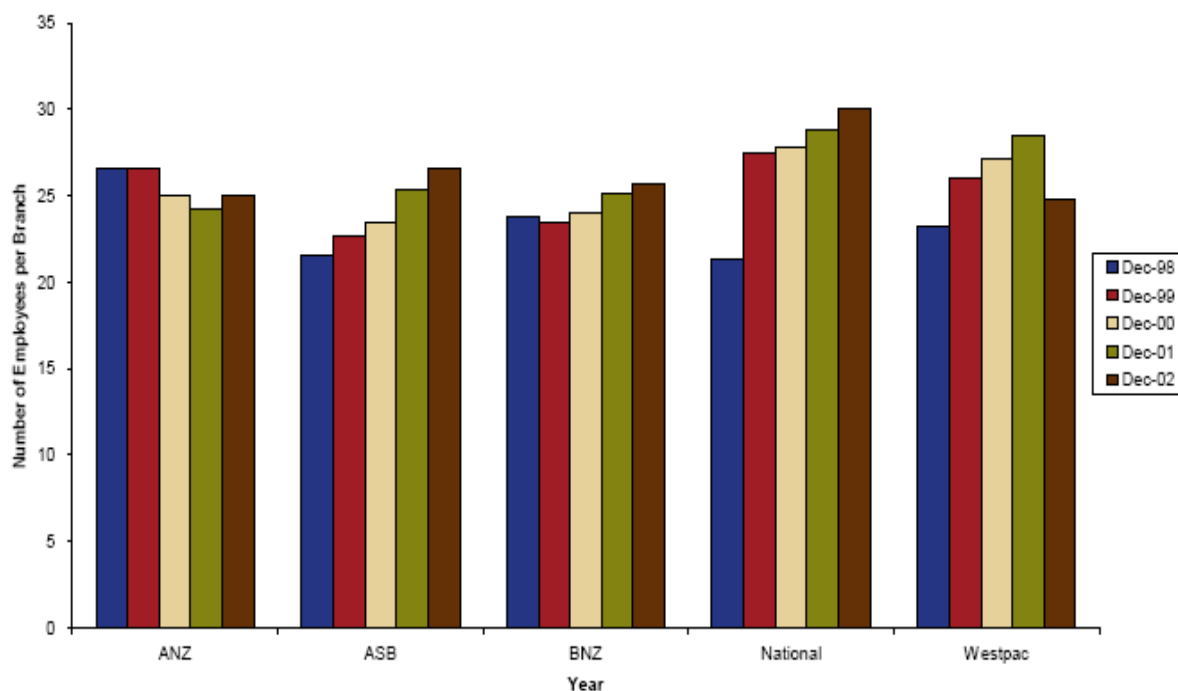
- There was a development toward increasing the number of employees per branch (please see Figure 10 - below), and the



number of SMEs per business manager was declining (Figure 11- below).

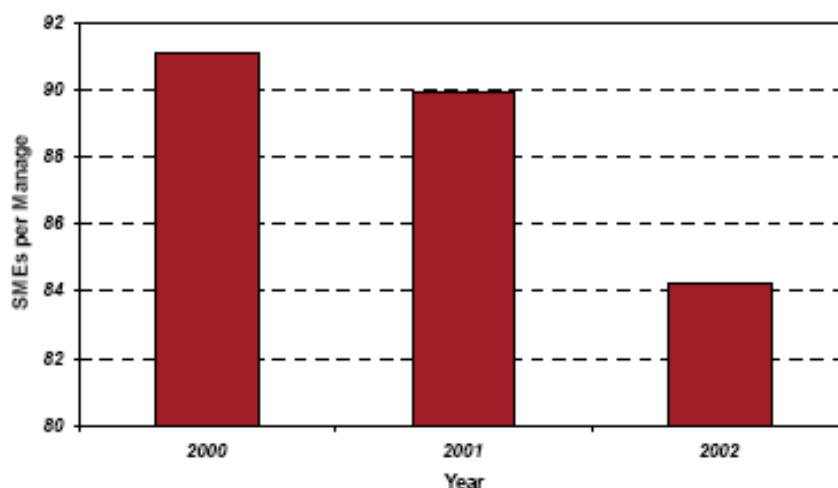
- The number of branches has remained fairly constant over the past four years in contrast with earlier years, when there were significant branch closures.
- And, as recently as 2010, the appointment of even more managers in the case of Westpac (Vass, 2009).

Figure 10: Increasing number of bank employees per branch



Source: Ministry of Economic Development (2003a)

Figure 11: Number of SMEs per relationship manager<sup>22</sup>



Source: Ministry of Economic Development (2003a)

Reflecting the wide practice of relationship banking by the five focal bank brands, in the New Zealand market, is the allocation of relationship managers to SMEs by region by two of the five bank brands (National and BNZ banks, for which data is publicly available) as at 2009. As Table 11 (below) and Figure 12 (below) illustrate, as the number of SMEs per region increases, so does the number of dedicated relationship managers.

---

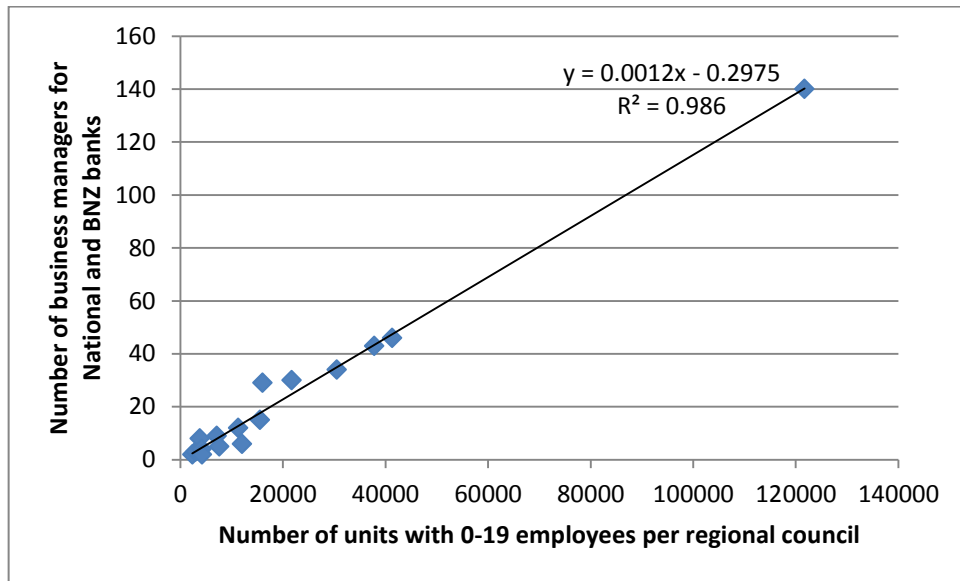
<sup>22</sup> It was difficult to find an up to date version of the table as the report from which it came was a one off exercise, however, table 10 and figure 12 shows a more recent correspondence between the number of SMEs and the number of bank relationship managers for two of the five major bank brands.

**Table 11: Number of SME units with 0-19 employees per region & number of corresponding business managers**

Region	Number of units with 0-19 employees	Number of Business managers	
		National bank	BNZ
West Coast	2338	One with Canterbury	1
Gisborne	2969	2	1
Tasman	3768		8
Nelson	4183	4	
Marlborough	4208	2	
Southland	7132	4	5
Taranaki	7608	3	2
Hawke's Bay	11318	7	5
Northland	12006		6
Manawatu-Wanganui	15554	7	8
Otago	16026	19	10
Bay of Plenty	21710	15	15
Waikato	30496	15	19
Wellington	37835	22	21
Canterbury	41288	18	28
Auckland	121692	61	79
Total	340131	179	208

Source: Compiled from multiple sources

Figure 12: Relationship between number of SMEs and number of relationship bankers per region



## IV.2 SMEs in New Zealand

Although worldwide SMEs tend to share some key characteristics, there is no globally recognised definition of an SME. Officially, in New Zealand, SMEs are defined as businesses employing 19 or fewer staff (Ministry of Economic Development, 2011). Typically, SMEs in New Zealand, like SMEs worldwide, are managed and operated by the owner, are not part of larger business groups and do not have any/many specialist staff, leading to a lack of access to managerial expertise.

The most comprehensive and regular report conducted on SMEs in New Zealand is produced by the Ministry of Economic Development and Statistics New Zealand. Every year, the “SMEs in New Zealand: Structure and Dynamics” report, now into its 12<sup>th</sup> year, aims “to provide a comprehensive picture of the current status of SMEs...[and offering] a statistical snapshot of the nature, structure and performance of New Zealand’s SMEs and larger enterprises, along with data on how they have changed over time” (Ministry of Economic Development, 2011, p. 3).

Looking at those 12 reports, New Zealand can and is adequately described as mainly a “nation of small businesses”. As of February 2010, nearly 90% of all enterprises employ five or fewer individuals, and about 69% of all enterprises have no paid employees (Ministry of

Economic Development, 2011). Table 12 (below) provides more detail on the number, percentage and cumulative percentage of firms by size.

**Table 12: Number, Percentage, and Cumulative Percentage of Enterprises by Size (February 2010)**

Employee Size Group	Number of enterprises	Percentage of all enterprises	Cumulative percentage
0	323,935	68.9%	68.9%
1-5	97,888	20.8%	89.7%
6-9	19,571	4.2%	93.8%
10-19	15,980	3.4%	97.2%
20-49	8,420	1.8%	99.0%
50-99	2,489	0.5%	99.6%
100-499	1,739	0.4%	99.9%
500+	324	0.1%	100.0%
<b>Total</b>	<b>470,346</b>	<b>100%</b>	<b>-</b>

Source: Ministry of Economic Development, 2011.

#### **IV.2.1 Importance of SMEs in New Zealand**

The importance of SMEs to the New Zealand economy can also be seen through a number of other criteria such as their contribution to employment, domination of most industries, and sales, profits and contribution to the economy's GDP. Each of these contributions is, in turn, sketched out below.

##### ***IV.2.1.1 SMEs' Contribution to Employment***

As is obvious from their numbers, SMEs make a substantial contribution to employment in New Zealand, accounting for between 30% and 31% of all employees during the last decade. The SME employment Table 13 (below) shows also that the workforce is comprised of 10.5% self-employed people with firms with five or

fewer employees making up 12% and the slightly larger firms with 6-19 employees accounting for 9.5%. (Ministry of Economic Development, 2011).

Table 13: SME employment in New Zealand during the last decade

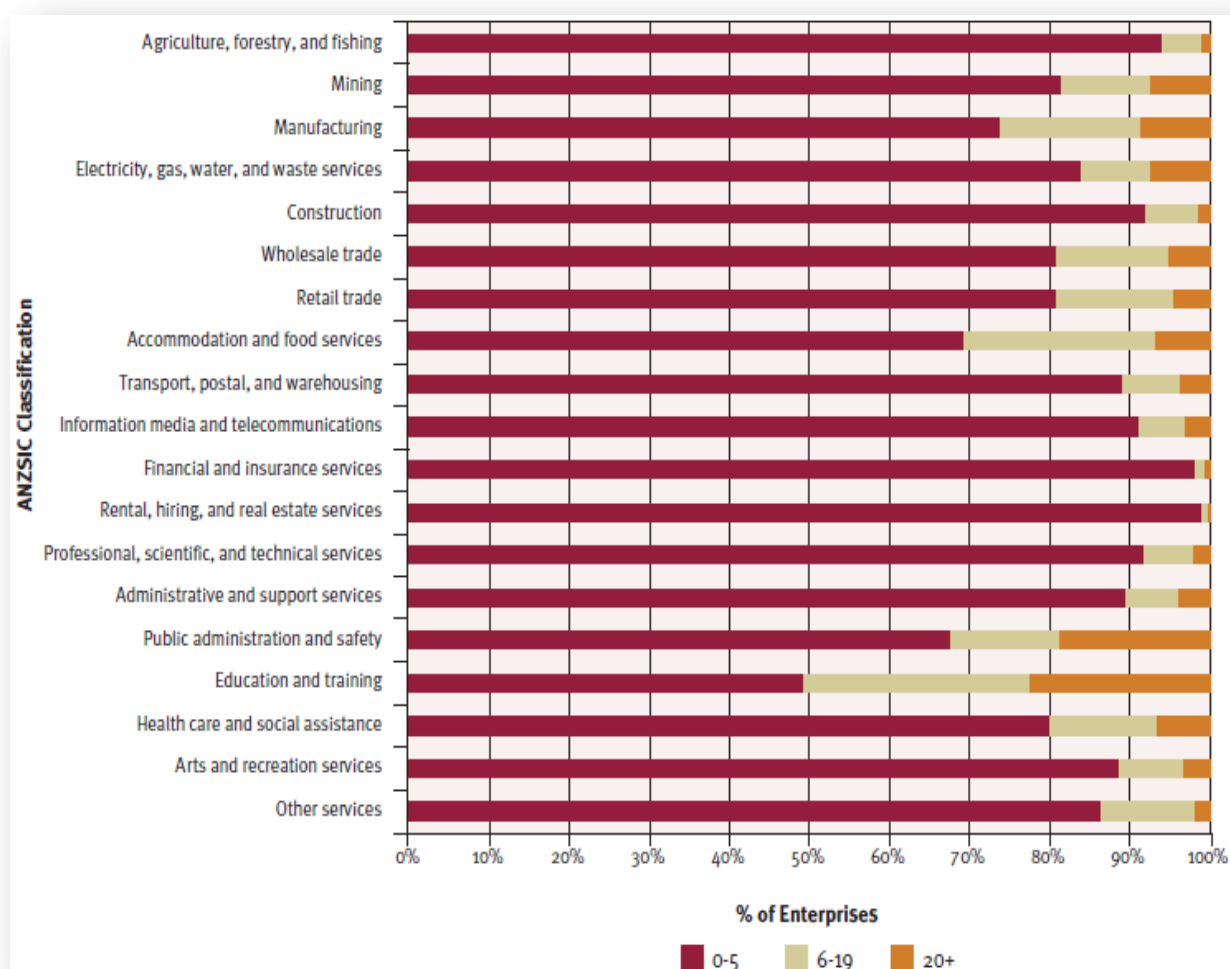
SMEs	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Total SME employment	503,240	523,990	545,510	563,530	583,180	591,400	598,880	606,970	590,560	580,680
Percentage change from previous year		4.1%	4.1%	3.3%	3.5%	1.4%	1.3%	1.4%	-2.7%	-1.7%
As a percentage of total employment	31.1%	31.5%	31.7%	31.4%	31.4%	31.3%	31.1%	30.7%	30.6%	30.7%

Source: Ministry of Economic Development, 2011

#### *IV.2.1.2 SMEs dominate most industries:*

In virtually every industry sector, with the exception of Education and Training and Public Administration and Safety, SMEs constitute over 90% of firms in New Zealand. However, there is a considerable amount of variation. From the percentage of enterprises by employee size group shown in Figure 13 (below), we can also see that SMEs are the majority in a number of divisions including Construction, Agriculture, Fishing and Forestry, and the Financial and Insurance Services (99.4%) (Ministry of Economic Development, 2011).

Figure 13: Percentage of Enterprises by Employee Size Group and ANZSIC (February 2010)



Source: Ministry of Economic Development, 2011

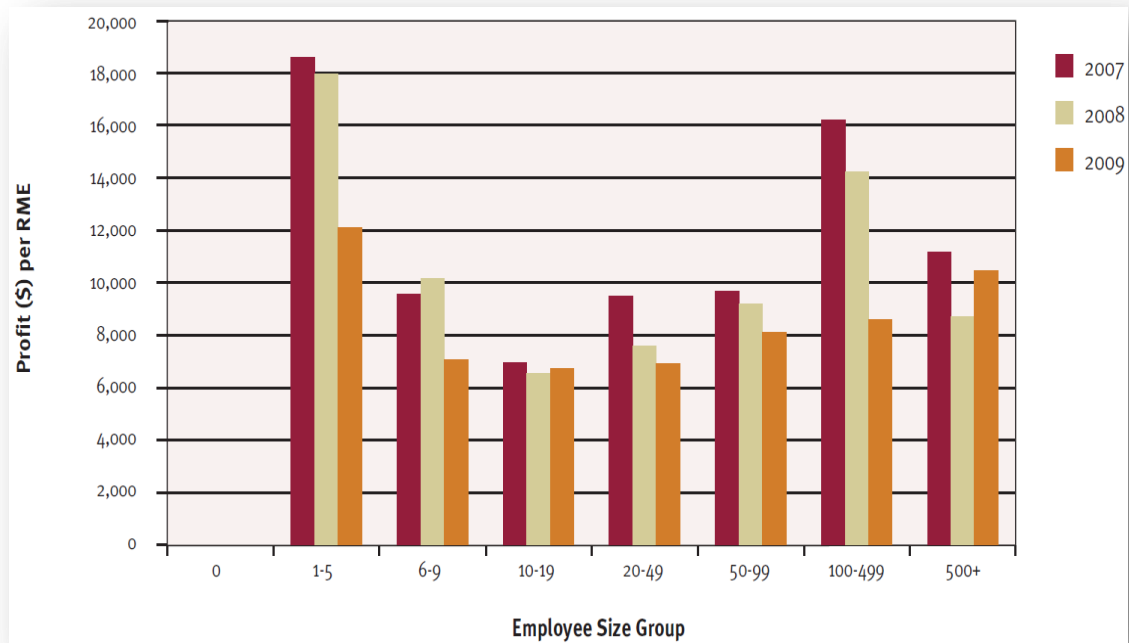
#### IV.2.1.3 SMEs' value addition to the economy:

Value-added measures quantify the contribution firms make to the economy's total output. New Zealand SME's value-added has been around the 40% mark during the last decade. Furthermore, through Figure 14 (below) one can see that "across all employee size groups, firms with five or fewer employees continue to generate the highest average real profits per employee, at \$12,132 (in 1997 dollars) profit



per employee (measured on a rolling mean employee – RME<sup>23</sup> – basis) in the year to March 2009. [Though], this profit level is a significant drop from \$18,634 in 2007 and \$17,974 in 2008” (Ministry of Economic Development, 2011, p. 8) which is likely to be an effect of the global financial crisis.

Figure 14: Average Real Profit per RME by Employee Size Group (March 2009)



Source: Ministry of Economic Development, 2011

Finally, the illustration of SMEs’ significance in New Zealand is not only through statistics such as those above, but also through the government’s involvement and actions as Perry et al. (2006) maintained back in 2006 stating that “the establishment of a Small Business Unit within the Ministry of Economic Development [MED] and the appointment of a Minister for Small Business are both

<sup>23</sup> A 12-month moving average of the monthly employee count figure.

indications of this increasing interest and commitment” (p.3) to the SME sector. Particularly, a number of programmes have been undertaken by the MED looking at the small business finance issues such as the ‘Bank Lending Practices to Small and Medium Sized Enterprises’ report (Ministry of Economic Development, 2003a), the ‘New Zealand's Angel Capital Market: supply side’ report (Infometrics Ltd, 2004) and the 2004 Business Finance Survey (Ministry of Economic Development, 2005).

#### **IV.2.2 SMEs numbers in New Zealand are no different from other OECD countries.**

From a comparative perspective, Duncan and Jason (2004) have raised the issue of how “almost all of the studies of firm dynamics in New Zealand have concluded that New Zealand has a very high proportion of small firms (and correspondingly low average firm size) by comparison with other OECD countries” (p. i). Two exceptions mentioned were the Ministry of Economic Development (2003b) study and Mills (2003) study. However, Duncan and Jason (2004) analysis reached a different overall conclusion stating that “once measurement differences are taken into account, overall New Zealand’s firm dynamics and demographics are broadly similar to many other OECD countries” (Duncan & Jason, 2004, p. i).

An example concerning the percentage of small firms in New Zealand from the Duncan and Jason (2004) study shows how their overall

conclusion is materialised follows. “The comparison in Table 14- (below) suggests that once zero-employee and one-year firms have been removed, the proportion of small firms in the New Zealand population is broadly within the OECD range. New Zealand has a lower proportion of small firms (90.7%) than do Finland (92.6%), Italy (93.0%), and the Netherlands (96.0%) – although it is not possible to be certain in the latter case, as zero-employee firms have been included in the Netherlands data. New Zealand does however have a higher proportion of small firms than Denmark, Portugal, USA, Germany and France. The size of the difference ranges from 2.6% (Denmark) up to 11.9% in the case of France. However, France appears to be something of an outlier, and this is probably due to the fact that the French business register applies a high turnover threshold – 3.8 million FFr per year in the manufacturing sector, and 1.1 million FFr per year in the services sector (Bartelsman, Stefano, & Fabiano, 2003). This high turnover threshold is likely to mean that many small firms would be excluded from the French data” (Duncan & Jason, 2004, p. 10). Duncan and Jason (2004) believe that the major reason for New Zealand firms to be considered remarkably small is that statistics which include zero-employee firms have commonly been included in studies when comparing to countries which do not count such firms.

Table 14: Proportion of firms with fewer than 20 employees, New Zealand & OECD firm project data

Country	Proportion
France	78.8%
Portugal*	85.9%
USA*	86.5%
Germany*	87.1%
Denmark	88.1%
New Zealand (NZ)	90.7%
Finland	92.6%
Italy*	93.0%
Netherlands	96.0%
NZ (0-emp/1-yr firms in)	96.1%

Source: Duncan & Jason, (2004, p. 9)

\* Private sector only. Note that if public sector is removed from the New Zealand data, the proportion of small firms rises to 92.1%.

A number of implications flow from Duncan and Jason (2004) overall conclusion. In general, policies based on the premise that the number of SMEs in New Zealand is relatively higher than the rest of the OECD countries “are probably not well founded” (Duncan & Jason, 2004, p. 10). In particular and in relation to the current thesis, small businesses access to finance and efficient functioning of financial markets are among the often quoted areas of calling for policy interventions. This is because those two areas are considered important in New Zealand due to the assumed higher number of SMEs in New Zealand relative to other OECD countries, and small businesses are informationally opaque, exacerbating the information asymmetry that exists between business borrowers and lenders as discussed in section II.3 above). However, the Duncan and Jason (2004), Mills (2003), and Ministry of Economic Development (2003b)

studies do not support this conclusion for New Zealand, suggesting that the problems are not any more likely to be acute in New Zealand than in a number of other OECD countries.

It is critical, at this stage of the thesis, to adequately discuss the context in which the New Zealand SMEs exist and, comparatively, how they have been discussed in various studies as Duncan and Jason (2004) have done. This is necessary as this thesis aspires to make analytical generalisations (as discussed in the methodology chapter, section III.2 above) and, in partial fulfilment of that purpose, specifically concerning the context a considered discussion of Duncan and Jason (2004) work is essential.

#### **IV.2.3 Importance of bank finance to SMEs**

The financial market in New Zealand offers a range of available sources of finance to businesses; however, banks are the predominant sources of external finance to SMEs (Robertson & Belanger, 2006). For example, in 2004, the Business Finance Survey conducted by Statistics New Zealand and the Ministry of Economic Development (2005) found that banks were the main source of current debt for nearly one third (32%) of businesses, followed by existing owners and trade creditors or suppliers, each counting for 25% and 24% respectively. Other results are shown in the current debt by source Figure 15 (below).

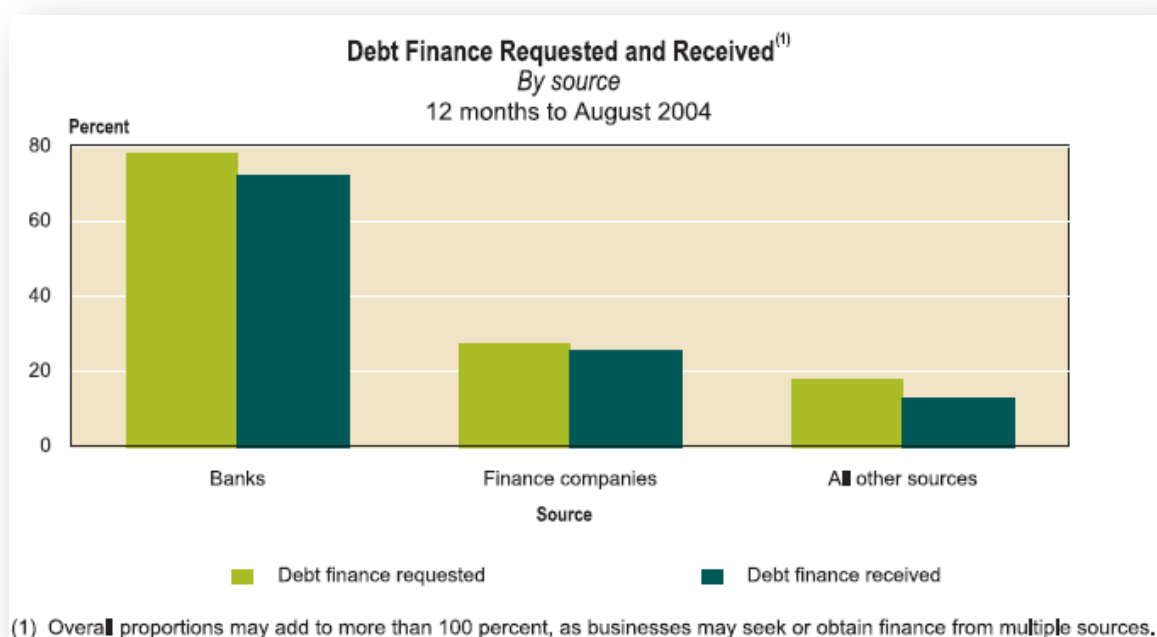
Figure 15: Current debt by source, last financial year at August 2004



Source: Ministry of Economic Development (2005)

Banks were also found to be important as the sources of additional debt finance requested and received in the 12 months to August, 2004. For 72% of businesses, banks were the source of debt finance received and finance companies were next in the line, but only for 26% of businesses. The full results are shown in Figure 16 (below).

Figure 16: Debt finance requested and received by source



Source: Ministry of Economic Development (2005)

It is worth noting here that, 1- the prominence of bank finance has remained more or less the same in recent years (Ministry of Economic Development, 2011), and 2- this is not limited to New Zealand. For example banks in the UK are also the predominant source of finance to UK SMEs (Irwin & Scott, 2010).

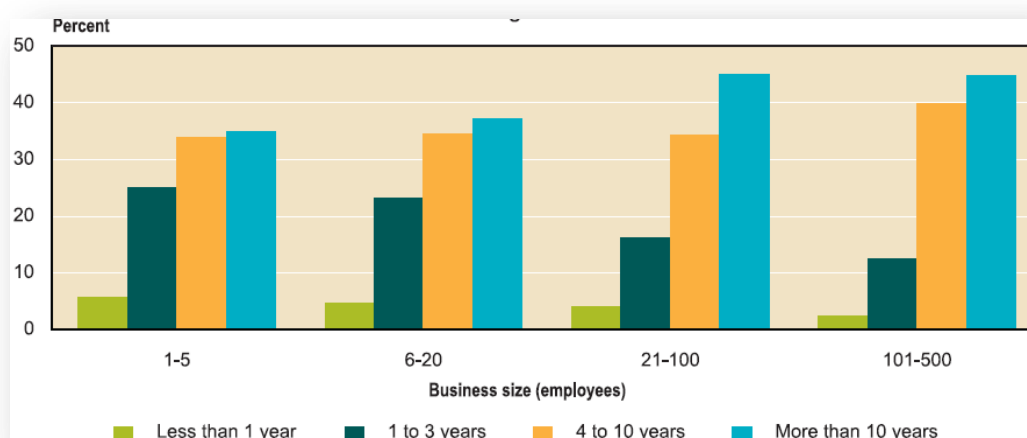
#### **IV.2.4 Small business-bank relationships:**

Despite the lack of research about some aspects of relationship banking in New Zealand, such as understanding the type of relationship banking that SMEs owners/managers develop with their bank (Perry et al., 2006), New Zealand small businesses appear to have relatively long-term relationships with their banks. This is supported by research such as Ministry of Economic Development (2005), Perry et al. (2006), and Robertson and Belanger (2006). For example, the Ministry of Economic Development (2005) survey found that 70% of firms had a relationship which had lasted at least four years and 36% for more than 10 years.

The bank-SME relationship was also found to be positively related to age and size of business, which is expected, given that larger firms tend to be older than small ones (Borrmann & Tripe, 2008). Looking at the 'years with main financial institution by business size' Figure 17 (below), 72% of firms aged between 6 months and 3 years were found to have relationship banking with their main bank or financial

institution for up to four years. In the category of businesses over three years of age, the relationship was four years or more (Ministry of Economic Development, 2005). Therefore, the banking relationship precedes the business start up, implying SME owners approach their own personal bank for business banking purposes, at least in the early stages.

Figure 17: years with main financial institution by business size



Source: Ministry of Economic Development (2005)

Finally, statistics about the length of the relationship with the main bank have to be carefully interpreted. This is because for a business, the length of the relationship might hide the fact that that business is unable to find an alternative financial institution to bank with or, due to the high costs associated with switching banking services suppliers, particularly for firms at the lower end, the business finds itself in a hold-up like position. Further research is needed to shed some light on this area.



## **Conclusion**

To answer the thesis research aim and questions, this chapter has looked into the empirical context of the study. The next two chapters report on the thesis findings, analysis and discussions.

## V. Analysis & Discussion -I-

### Introduction:

This chapter and the next cover the research/thesis findings, analysis and discussions.

In these two chapters, findings are presented first, with verbatim evidence from the interviews extensively used and presented both in *italics* and indented. On occasion, the researcher's questions are also added (in **bold**) to enhance understanding and provide context. The findings are then analysed and discussed in light of some of the relevant literature. Overall, emphasis is on processes and mechanisms, in line with the overall objective of the thesis research aim/problem and questions, being to investigate the sources of benefits from relationship banking accrued by the five major bank brands in New Zealand when dealing with their SME customers and the processes/mechanisms for securing these benefits.

The current chapter begins with section one, which reports on how banks organise their activities by way of segmenting their markets into clear categories including the SME segment. Then, section two provides an analysis into how banks define SMEs. Section three elaborates on the clearly identified taxonomy of the SME-banking relationship management models used by banks. Then, section four details banks' lending approaches and criteria used to assess loan

applications from their relationship managed SME clients. Section five reports on the essence of relationship banking to the five bank brands sample of the study. Finally, section six concludes the chapter.

### V.1 Banking segments:

The interviews revealed that banks divide their activities into two main categories; personal and business. The business banking segment is further divided into sub-categories. While different names are used to refer to these sub-categories by the different banks, the majority of interviewees (22 out of 27) have explicitly expressed this idea, which was well captured by interviewee 9:

*We have two, well three, quite separate divisions within the business banking, and the first division is what we call small business. We call it our business banking unit which basically is any business wanting to borrow up to a million dollars. So that's what we call the small business. Then we have what we call commercial banking which does anything over a million dollars' worth of borrowing and then after that we have other sort of specialist areas where we have corporate banking who look after our corporate stuff, yes. For example like [city's name] airport that would fit within Corporate Banking and the other one is property financial unit which specialise in commercial property; either large commercial property investments or commercial property developments. 1/9<sup>24</sup>*

The cut-off points between the different segments also vary between banks. A reasonably common division is along the lines of:

---

<sup>24</sup> 9 refers to interviewee's number, and 1 refers to the page number of the transcribed interview from which the quote was lifted.

*Businesses up to \$250,000.00 lending would be small business. That's just a small business. Medium size business we'll call them shall we for the next one... That's \$250,000.00 to a million, and sometimes it can go up a little higher than that but say, two million and above. Two million above, that's probably what we call large businesses.*

***Corporate?***

*Yeah. That's lending corporate, corporate customers. 2/3*

Referring to small business, the same interviewee 3 added,

*And there is even one category below that which is about 50,000.00 fifty thousand business lending and that's the small, small lending.*

***Oh is that micro kind of [business]?***

*Yeah. Micro, we'll call it that. 3/3*

Banking to the small and medium sized enterprises (SME) is divided into three or four segments. Again, this idea was articulated by the majority of interviewees (21 out of 27) and according to interviewee 13,

*We've got segmentation under business, so it's actually like that. It's got, we call them micro, and then package, and then custom.*

***What's the difference between...?***

*Probably borrowing up to 250,000.00 five hundred thousand up to a million and then over a million. Over a million up to custom. 2/13*

Another bank uses different names as explained by interviewee 2:

*In the bank we have the online business, small business, business manager, and relationship manager. Four, four ah, four segmentation in business banking. 14/2*

As with the previous classification of businesses into categories such as corporate and commercial, it is clear from the interviews that there is considerable variation between the five bank brands in terms of what cut-off points in the criteria they use to segment banking to SMEs. Some of those criteria are the amount of lending to the business, complexity of the business, and turnover of the business. For the purposes of this thesis, however, the following classification, judged to be operational, when banking to SMEs will be used:

- Online banking which is charged with managing those businesses that are very small and/or don't have much borrowing, and as explained by interviewee 2 saying:

*Don't need a lot of personalised service; they need fast and convenient service. 14/2*

- The next segment is small business banking. It deals with businesses with borrowings of up to \$250,000 in the case of BNZ and only up to \$50,000 with ANZ. The last segment, business banking, deals with medium sized enterprises with borrowings of up to \$1 million with the ANZ bank, and as high as \$3 million with BNZ.

The classifications used by the banks aim to facilitate the efficient management of their customers and their activities. Their framework is captured in Figure 18 below.

Figure 18: Segmentation of the banking activities by the 5 major banks

	Banking				
1 <sup>st</sup> classification	Personal	Businesses			
2 <sup>nd</sup> classification		Small to Medium Sized		Corporate & Commercial	
3 <sup>rd</sup> classification		Online	Small	Medium	

## V.2 Small business definition:

For the purposes of this thesis, there has been no attempt to apply rigid criteria to define a SME. Various taxonomies are available from governments (Ministry of Economic Development, 2010) and international organisations (OECD, 2004). “However, the main criterion that OECD countries, including New Zealand [to define an SME], use for statistical purposes is the number of persons employed” (Ministry of Economic Development, 2010, p. 93). These parameters have not been applied and, from the definition of SMEs as distilled from the interviews, it is apparent that the banking approach may differ. The way in which the interviewed bankers defined small businesses is shown in Table 15 below.

Table 15: Criteria used in defining small businesses.

Criteria	Type
Sector of activity	Qualitative
Complexity	
Ethnicity of the owners\managers (recent)	
Primary source of business owner's income: over 50%	Quantitative
Turn over	
Business lending .... Amount of exposure	

Banks use several criteria that reflect a multidimensional frame of reference. These criteria are used in tandem and the main ones can be reduced to six questions with three having a largely qualitative response and the other three being more quantitative.

The reason for using these criteria is first to classify businesses into categories and then decide how a particular business is going to be managed, i.e. which relationship model<sup>25</sup> and then finally, may be, particularly in the case of small to medium sized firms, which business/relationship manager will be in charge of managing the relationship (on behalf of the bank) between the business and the bank. The rest of this section consists of a detailed discussion of these criteria.

---

<sup>25</sup> Please see details about this in section V.3 below.

### V.2.1 Sector of activity:

Banks classify their SME customers by sector of activity in order to facilitate their management. This can be seen clearly through interviewees' comments about the types of businesses they manage, such as interviewees 1 and 22:

*I don't do any Agri[culture business] stuff; across industries but not farming. 2/22*

***Your customers are across different sectors.***

*Correct.*

***Farming?***

*No farming.*

***How about Property Developers.***

*I haven't got any Property Developers or Real Estate agents on my set. 3/1*

Certain aspects within some sectors of activity such as real estate are (or appear to be) specific to those sectors, and the bank manager who has been dealing with SMEs from one of those sectors would accumulate knowledge and expertise that would prove to be useful in the management of these enterprises. Further, banks are able to develop and offer financial packages tailored to a specific sector's needs, therefore contributing to the efficient and optimal use of resources.



Allocating businesses into industrial sectors is also essential because the rest of the criteria are not equally applied to all businesses. A real estate business with a turnover of three million dollars would be considered a micro to small business from a bank perspective; however, a sophisticated software developer with the same turnover would be viewed as a complex business to the extent that it would be managed by a business manager in charge of medium-sized businesses.

### *V.2.2 Complexity of the business:*

The complexity around the business activity is another dimension of the banks' definition of SMEs as explained by the interviewee 12 when answering a question about what is an SME:

*Depending on the profitability is one key factor for us, so depending on the profitability, the size of the business and the complexity; that will dictate whether they get a one-to-one business manager or a one-to-many 2/12.*

The software development company that deals with a number of customers and suppliers, each located in a separate country, would require the business manager in charge of the business to have some level of understanding of Forex, the software industry and international trade. This business complexity aspect is decided irrespective of the small business turnover and/or amount of borrowing, although those businesses with lower amounts of

borrowing tend to be less complex and vice versa as explained by interviewee 4:

*I would say if they're borrowing quarter of a million off us they'd be fairly complex entities. 33/4*

### ***V.2.3 Ethnicity of the small business owner/manager***

The last qualitative criterion, ethnicity of the new migrant small business owners/managers, is a relatively recent defining factor, and is used by all five bank brands participating in this research. Interviewee 1 explained briefly the rationale behind this move by his bank.

*We've actually set up Chinese business managers and it's primarily (a) for the language issue and also their understanding of how they operate is probably a lot more better than what I would be able to do. 19/1*

However, not all ethnicities are considered; only those with SMEs large enough in number to represent a lucrative and viable market segment for the bank and warrant dedicated business manager(s). So, currently, only some Chinese and Indian small businesses communities located in some of the main business areas of New Zealand are served by this migrant business banking.

### ***V.2.4 Primary source of income:***

The first of the quantitative criteria is related to the business' capacity to generate enough income for the business owner/manager (O/M) to

live on. In other words, the business has to be the primary source of income for its owner, as explained by interviewee 20:

*We manage all our SMEs, unless it's a very small hobby business. So, you know, if it's not the person's main income then that will probably just not have a business manager. 14/20*

#### **V.2.5 Turnover:**

Defined as the total value of goods and/or services sold during one financial year, the turnover is first used to categorise the bank clients into three distinct groups of customers: SMEs, mid-market, and commercial. Then, within the SME group, businesses are further subdivided into three subgroups and these are micro, small, and medium sized businesses. Interviewee 15 explained about the turnover and number of employees criteria of his SME clients saying:

*Generally I'm seeing businesses with turnover up to five million and staff under 20. 2/15*

#### **V.2.6 Business lending:**

Finally, from a relationship banking point of view, small businesses are approached as *groups* adding the small business owner/manger's personal account and at least his/her partner's into the business account, as explained by interviewees 15 and 3 respectably when they said:

*From our point of view we group customers together so where – and it can get quite complex- but where there's a business being*

*run jointly between a husband and a wife or even the wife's running a business and the husband's off doing something else, we look at their whole income picture. 4/15*

And,

*We group our customers together. So, how we manage it we may have; take you as a group so you're one party to it but all your associated accounts, your personal accounts of you, your partner etc. 5/3*

### **V.3 Taxonomy of the business banking<sup>26</sup> relationship management model**

Within the small to medium sized business-banking segment, interviews have shown a clear taxonomy of relationship banking.

Interviewee 3 elaborated on this saying:

*We kind of tend to split them [businesses]. I don't know what others do but we kind of split them; there is a business manager who takes care of that fifty group. I take care of the two-fifty and another man here. So we just split it that way.... Because I mean in the bank, you know, we call them - like a person who does that fifty - we call them small business manager; we call me a business manager and we call the other manager who does two-fifty a relationship manager but that is only just purely for terminology. 3 & 7/3*

As with the previous classifications of banking to businesses, the cut-off points of this taxonomy vary greatly between banks, as can be seen from what interviewee 3 said when compared, for example, with what interviewee 14 from a different bank said:

---

<sup>26</sup> From this point on, banking to SMEs will be referred to as 'business banking'.

*At the [bank name] there's sort of three tiers I guess of lending so our micro business managers do up to 250,000.00 of lending then our package managers do up to one and a half to two million of lending, and then I [customer manager] do two to about fifteen million of lending. 2/14*

According to this taxonomy, businesses are allocated to a bank relationship manager who manages the relationship with the bank. As businesses and their banking requirements grow, they are transferred to the next level up in the relationship management ladder to be managed by a business manager. Interviewee 3, by way of a real example, explained this issue saying:

*I just have a customer who (I can tell he does have a Paper Plus), so I've helped them and they're going to buy another one and two of them. So, the lending is gonna be a colossal bit more, so I pass them onto another manager, and the reason being is that that manager also requires to do a little bit extra because they, and he has the skills. And also he has, what we call in the business, the ability - we have lending limits.*

***Oh, discretions...***

*Discretions, yeah. 51/3*

Just as the skills required to manage businesses vary from one level to the next, resources available to the bank managers such as cars to visit clients, discretion levels, and levels of support were found to differ too. These differences were even reported to be present between the individual business managers at the same level at the same bank, depending on the level of experience and other considerations.

Details about the three levels of relationship banking follow.

### V.3.1 Online management model:

Micro businesses and some of the small ones, sized below a certain threshold and/or with borrowings below a certain level, are managed online and/or by phone via a call centre and/or a local bank branch. Some of the interviewees (6 out of 27) referred to this model as the ‘online business’ model while a few of the others called it a phone proposition. Interviewees 3 and 5 respectively said:

*What we do have is what we call online. So, anyone who opens a business account, and it reaches a business account, it goes to our online team. An online team is just a 0800 number and they will assist. So, they ring a 0800 number and say ‘I want an overdraft’ and it’s done over the phone or everything’s done over the phone. When you get over 20,000.00 lending you come to a business manager and the reason being is it requires perhaps more expertise...they look after about twelve hundred [customers] or more. 30/3*

*So the very little businesses that maybe have no borrowing needs – just want a business account – they are assigned a person who is their business manager but he will be mainly a phone proposition.*

***Oh, so, if a business was from Hamilton as you’ve described, the business would not be assigned somebody from here?***

*Yeah. It would be probably based in Auckland phone proposition. 17/5*

Under this model, information about those online businesses is kept in files in a central computer in a call centre in one of the major cities such as Auckland. A team of bank managers is also based in that call centre. When the small business owner/operator calls the call centre,

for example, for a banking product and/or service, any business manager who happens to be free and is online will deal with him or her. It is as if a number of online business managers collectively manage a set of online businesses, hence this thesis is proposing a *many-to-many relationship management model* as a label for this type of relationship banking model.

None of the online business managers at this level seem to have any discretion beyond a small amount of lending like that granted under a business credit card or a small overdraft. Finally, though interviewees have expressed a range of opinions regarding the number of businesses per business manager depending which bank they are working for, the number of clients seems to be higher than 1000 for every online business manager.

### **V.3.2 Small business relationship model:**

All interviewees said that as some small businesses grow, their levels of business activity, complexity and sophistication grow as well. The volume, the kind of banking products and services, and the level of bank involvement and management need to match this growth. The banks' response to these changes is then to provide a one-to-one business relationship-banking model. Interviewee 8 explained this issue:

*We see it like a pyramid; we deal with the volume ones as we come up the pyramid. And ah, these customers hopefully will continue to grow and they'll become commercial clients for the commercial managers or they'll become property finance company for corporate managers; we've got all sorts of processes within the bank, all sorts of specialist areas.... As they keep on growing, the level of sophistication we can pass them on to appropriate specialists as required. But I mean we, we ourselves use specialists through the normal course. We've got trade finance specialists. We've got merchant service specialists. We can use that; I can still manage the relationship and use these people. Okay? But there may come a point where they are, their exposure is big enough and this level of sophistication is big enough that I will pass it on to someone else who's got more resources and more specialist knowledge.*

***Oh right, and that's it? Finished this relationship with you?***

*Relationship - pass it on to someone else. 20-1/8*

Each and every small business is allocated to a designated/specific small business manager, henceforth called business manager. Each of these business managers is physically located in one of the bank branches around the country, and is responsible for managing his/her customers' relationship banking with the bank. These business managers are the main point of contact between the bank and the small business client. While the number of businesses per business manager seems to vary greatly from bank to bank, on average it is much less than that of the online business manager. This seems to be a natural outcome of the nature of relationship banking at this level, as more time and expertise are required of the business manager to cater properly to these types of businesses, which includes visiting their work premises.



According to the very few interviewees who elaborated on the issue of discretions given to the different bank managers, and in comparison to the online-business managers, the business managers enjoy higher levels of discretion, including dollar-lending discretion; however, this comes with provisions. The discretion levels vary from one manager to the next and tend to be given to the individual not the position.

Interviewee 19 elaborated on this issue saying:

*So even if the computer system were to prove something, the staff still have the ability to say no, and if it doesn't approve it we still have a place what we call a discretion which allows us to approve up to certain levels and that's often based on experience levels, and then you can approve something within that discretion. 5/19*

The business managers also have access to more resources and support. The support model used at this level is that of one-to-many where a credit analyst, for example, is shared among a number of business managers as explained by interviewee 12

*For example, in behind me my support mechanism I've got one-to-many, so I go to a team; different credit teams and different people that support me. Whereas the next tier they'll have individual analysts and support people working with them. So they have, like a manager, assistant-manager and so on like that.3/12*

Furthermore, the interviews identified the existence of special business managers dealing only in specialist markets, such as franchising, and with new migrants groups such as Chinese and Indian. With franchising for example, and because franchising is a

proven model of business, banks have developed predetermined packages aimed at some of the franchising businesses, which are then managed by a franchising business manager. This point was well explained by interviewee 7 when asked about the different segments within business banking that his bank splits its customers into.

*Franchising, we split off franchising.*

***So there's a business manager who looks after only franchises?***

*We've got a franchising business manager.*

***Okay and that's different franchising like restaurants?***

*I mean franchising is a little bit of a specialist market because generally the bankers, because they are proven models of business, banks have packages in place that they will actually, ... predetermined packages in place that they will lend to those businesses. 'Cause they're consistent, they're all the same, so it's easier, every other business has differences. 18/7*

### **V.3.3 Medium sized business relationship model:**

At the upper end of business banking and across all the participating banks, there are the managers of medium sized businesses, henceforth called relationship managers. On average, these relationship managers are in charge of a portfolio of businesses numbering less than half that of a business manager. Furthermore, relationship managers have discretion levels with upper limits much higher than those enjoyed by the business managers and reaching as high as five million dollars in the case of interviewee 13.

*In the office we can do ten million [of lending] because our credit manager and me can do five each... I can do five myself without talking to anybody and together we can do ten. 9/13*

These discretion levels are also granted to the individual relationship managers rather than to the relationship manager position.

From the interviews, the relationship managers are expected to be more proactive in their approach with their customers in terms of keeping in touch with them via phone and emails, visiting their work premises, and initiating deals. Whereas the business managers are more reactive to their customers when it comes to contacting them and/or when needed, following the “set and forget” guide. The relationship managers are also expected to know/learn about their customers more intimately than the business managers and to deal with them face to face. Interviewee 4 captured this issue of proactive and reactive well when he said:

*My expectation is my manager's that live in that space, and to a certain extent all my managers do but mainly the junior ones. They get reports out and they do reviews on those things that come up in the report. So, they're flags that come up out of that information. So, whilst I expect them to be doing call and care with their customers on a fairly regular basis – most of their contact is dictated by computer generated reports. Which look at, look at outriders really, or flags. And, and, and – so we're reacting to something rather than being proactive. My senior managers are being proactive...*

*My expectation, you know in an ideal world, my expectations would be for my managers to proactively contact the customers every quarter. Whether by telephone, whether by letter, whether by actually, physically meeting them. Um – my expectation is,*

*there is some contact point, and there is some proactive contact. In other words we, as a lender, turn up and say, "Hello Alan. How's your business going?" Okay? So, so there is conversation taking place. Um – in, in; annually – at least annually, there is a discussion about the position of the company, about the products that they have, that they're using from the bank and whether we can add any value to them.... Um – and my expectation of my senior manager is that they would visit everybody's premises once a year, to get a feel. My junior managers can't do that. They've got too many customers. 37-8/4*

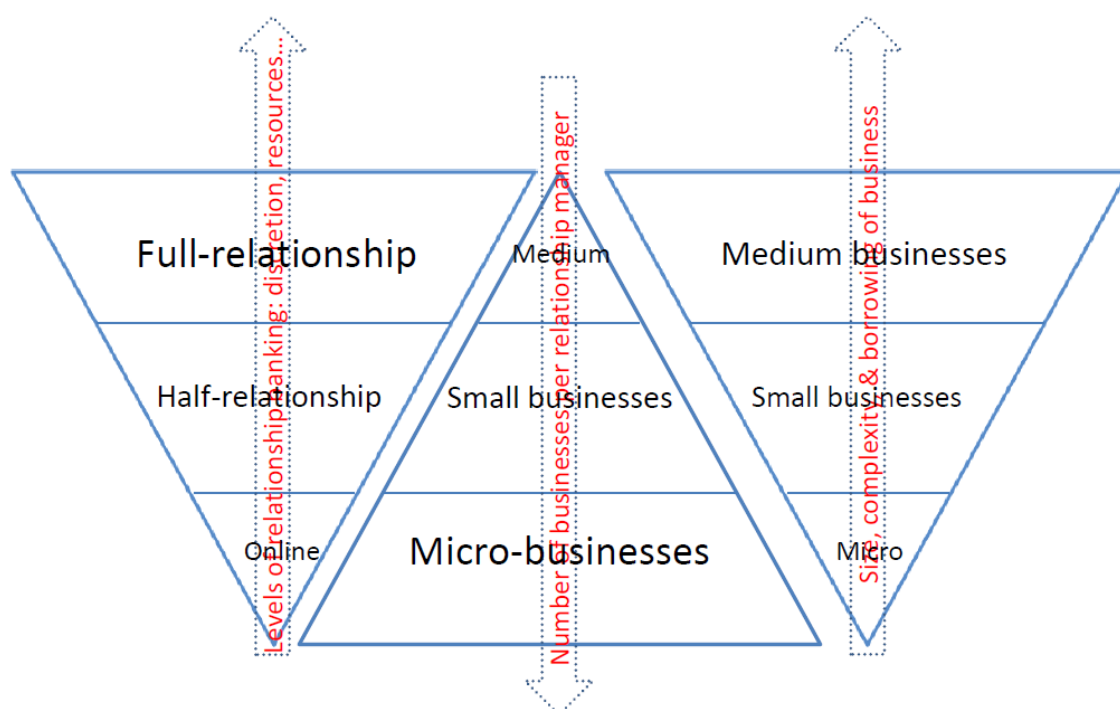
All of the relationship managers and some of the business managers have an account manager or an assistant manager who is in charge of the day-to-day management of the business account and who look after things such as their term deposits and maintenance queries, because once a loan is contracted the clients want banking to be easy. The relationship manager is called in only when big things are happening, such as new loans, in which case the relationship/business manager gets involved until the deal gets approved, gets it all through to the solicitor for documentation, and then the account manager picks it up and does the rest. This frees the relationship/business manager to attend to bigger and more profitable tasks from the bank's point of view. Interviewee 8, who is a business manager, stated:

*I'm the business manager but I have account managers who look after the business on a day-to-day basis. If I get involved meeting the people for the first time, looking at a proposal, making sure that I - we don't proceed with a lot of them. So that, say, two out of ten that we'd proceed with. We see a lot of stuff that we don't go any further with. So, those ones that have decided that it's worth it, I can either approve them myself or send them to the bank for confirmation. So, I'm involved to that*

*point in getting it all through to the solicitors to get it documented and then my account manager picks it up, introduces themselves and they do a profile to make sure all of the needs are covered and they are the first point of contact.*  
15/8

Figure 19, below, summarises the three levels of relationship banking within the small- to medium-sized business banking segment.

Figure 19: taxonomy of relationship banking within SME banking



The left triangle represents the level of relationship banking (in terms of discretion level given to the relationship manager, resources at his/her disposition to use such as a car...) it is an increasing function of the type of relationship banking going from online (where the relationship manager has minimal discretion and resources, if any) to half relationship banking then to the full relationship where the relationship manager is granted the highest discretion in SME banking. The middle triangle means that the number of SME clients

per relationship manager (in his/her portfolio to manage) is a decreasing function of the type of relationship. Going from online to full relationship the number of SMEs to be managed decreases. Finally, the triangle on the right is to say there is an inverse relationship between the size, level of complexity, the amount of borrowing and the type of relationship banking that the business will have. As size of the business increases going from micro, to small to medium – this coupled with the complexity of the business and more borrowing, relationship banking model used will go up from online model to half and then finally to the full relationship banking model.

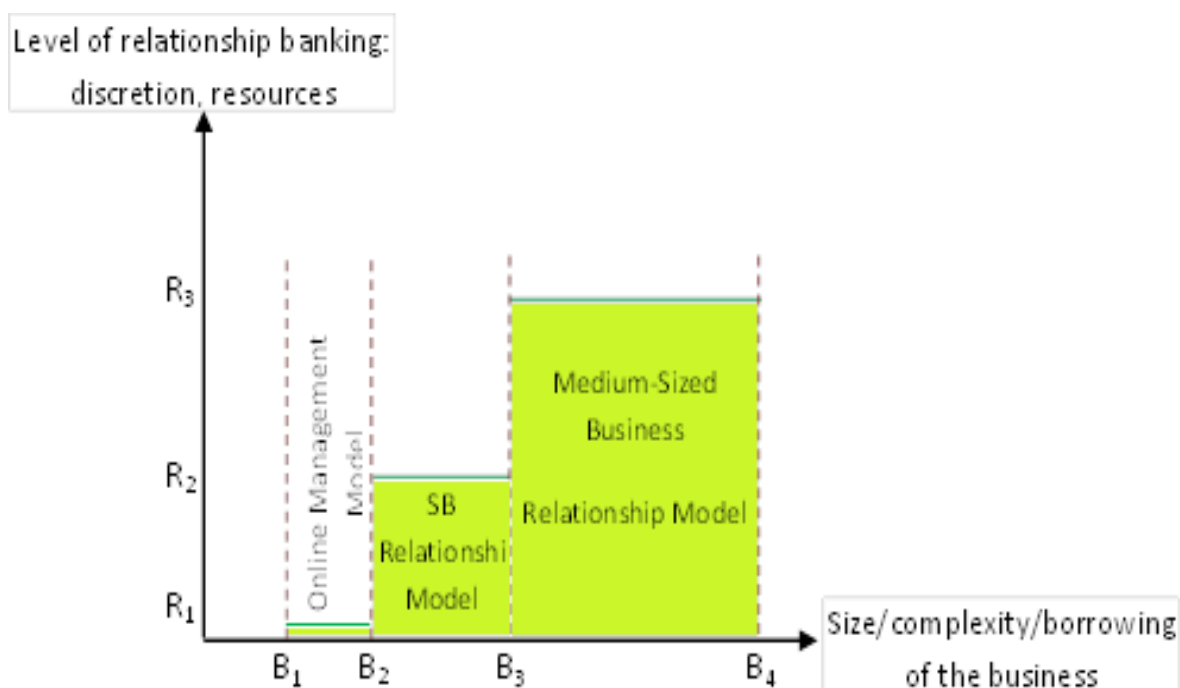
From a brief review of the literature on relationship banking, such as those by (Bharath et al., 2007; Boot, 2000; Brown & Zehnder, 2007), it quickly becomes evident how relationship banking is approached as if there is only one type of relationship across, and with, all types of businesses, small (Cole, 1998; Peltoniemi, 2007; Perry et al., 2006; Petersen & Rajan, 1994; Scott, 2006; Uchida et al., 2006) and large (Billett et al., 1995; Hoshi et al., 1990; Lummer & McConnell, 1989; Slovin et al., 1993). These studies do not clearly differentiate between possible different types and levels of relationship banking. The widely

used definition by Boot (2000) is an example of this reflex, however implicit it might be.

However, the current study's findings have shown the existence of levels of relationship banking with clear demarcations between those identified levels. The amount of working time that a business manager can dedicate to an individual client differs from one level to the next. The level of resources available to the business manager, such as a car to visit the client's work premises, also varies between levels. Furthermore, differences are not limited to a bank's inputs and associated costs (per client from different levels), rather, and as an expectation from the bank's perspective, the benefits and amount of return realised per client are also different.

The three segments of relationship banking identified by the current study and the types of businesses in each segment can be formally modelled to distinguish between the segments in terms of types of businesses at each level (as well as costs and benefits associated with each segment). The main points of this model are highlighted/depicted in Figure 20, below.

Figure 20: stepwise function representation of the different segments of relationship banking



Distinguishing between the different segments of relationship banking is essential from a number of viewpoints. One, because the relationship cost function is different from one level to the next, the return function would also be expected to be different. Banks would want a return function commensurate with the cost function related to each segment. Two, a proper evaluation of each segment requires a clear distinction between inputs/outputs associated with each segment. Finally, in terms of investment decision making, for a bank to choose between the three levels of relationship banking, the amount of limited resources to dedicate to each segment for an optimised use of those resources, and/or to make the necessary changes to its model of



management, the bank needs to conduct a separate cost-benefit analysis for each segment.

In point of fact, a few interviewees reported changes to one of their relationship banking segments their banks were either planning or implementing. This was as a result of evaluating a segment via cost-benefit analysis. More precisely, complaints were registered and concerns were raised by some interviewees about the high number of clients per business manager – particularly in the small business relationship segment. Interviewee 14 said:

*I guess though, the smaller the business it becomes harder to do because they've got less time to dedicate to each individual customer. 15/14*

Interviewee 4, a regional manager, explained this further:

*Some of those managers, ah, 40% of our book are managed by off-site on what we call online banking. So their managers sit in a building in Auckland ah, and they're managed over the telephone from Auckland. Ah, so not all person-to-person? Yeah, so that's businesses under twenty thousand without a mortgage. They're not person-to-person. So 60% of our customers and um, business customers either have a mortgage or have lending over twenty thousand dollars, are managed; they have a person dedicated to them. So the other 40%. Now the A bank which is our, um, which has the highest customer satisfaction in New Zealand has 60% of their customers managed by a telephone. But again are all dedicated managers. B bank, our competitor at the moment is hiring, is hiring front line managers to do exactly what we're doing to try and replicate what we're doing. We believe the C bank are setting up an online team to try and replicate that as well. So we, we think the model is um – you need a dedicated manager. Does the dedicated manager have to see you face-to-face? No.*

*I think that the cost income ratio on that, or cost, cost benefit ratio on that, um – there, there is a point where it's just not feasible and it's better to have them all banked up in on the telephone. Um – in fact, our customer satisfaction for those guys who are being looked after by a dedicated person on a telephone are actually higher than my small business managers who are meeting them face-to-face because my guys are buried basically and only can give so much time. The guy on the telephone has got, he's – no distractions. 52-3/4*

The reported changes looked like a further shift to phone-based management of those small businesses managed via the small business relationship model, rather than hiring more business managers, as was reported in the case with Westpac (Vass, 2009).

#### **V.4 The lending approach and criteria used by banks to assess SMEs' loan applications:**

This section reports the interview findings on how banks process loan applications from their SME clients. This is critical because to be able to identify the true sources of relationship banking value addition we need to know the place and the contribution of relationship banking in the overall process of lending in terms of approach and criteria used by banks to assess SME's loan applications and decision making. Bharath et al. (2007) and Ergungor (2005) studies didn't do that which renders their findings bit questionable as the benefits or lack of them they have identified could easily be attributed to the other lending technologies that banks use in tandem to process loan applications from their clients. Hence it is first step towards a proper assessment of

relationship banking benefits. From comparing the interviewees' answers to the questions about how they assess loan applications from their SME clients, there seem to be no real differences between banks as far as the lending criteria and processes used. The only differences that may exist will take effect mainly as consequences of the different discretionary limits that the business/relationship managers enjoy, and cut-off points between the different banking segments discussed earlier.

It is obvious from the interviews that there are three criteria, similar among all banks, for assessing a loan application from an existing relationship-managed SME client.

- 1- Lending is done on a cash flow basis, i.e. by assessing the client's ability to service the loan from the cash flow generated by the business.
- 2- While security is a requirement, it is only used as a second exit and a backup plan in case the SME fails to meet its payment obligations from the cash flow.
- 3- Assessment of the SME owner/manager, referred to by most interviewees as character, is as important as cash flow and security.

Reflective of the interviewees' consensus on these points, interviewees 6, 7, and 8 respectively said:

*We really have the three things. I mean everyone looks at people at all different ways but from a bank's perspective the way I've always looked at it is that you look at, and in no particular order, you look at the ability to repay. That's vital because as you're probably aware, banks have a duty of care. If we breach that we can be sued, so that's absolutely vital.... I mean servicing is a big one and then the other thing that the bank would look at, you look at the security. That's the other thing, and the third one, which is also very important, is the character of the customer as I've heard is, what's the standing of this person, what's their statement of position like, what's their lifestyle, what's their credit history like, all those sorts of things. So, those are really the three main things that we take into account and I mean from my perspective you view, you really need to be satisfied in all these. 4-5/6*

*Because that's what's important at the end of the day when you lend someone the money the key thing is that that person can repay that money. That's number one, the second thing is the security side of it, yes that is important but the weight here is in most cases probably less. The weighting through credit scoring will be less than they've got the capacity to repay. And the character. 20-1/7*

*Basically two things we look at are security and serviceability. Obviously security is your [collateral]. And your serviceability is your finance. And then obviously the relationship part of things is, is making sure the credit checks don't come up with anything too adverse or anything of that nature. But, but those are two objective ones if you like, that's security and serviceability. And if that's coming through all right and the person checks out all right; that's the third one. That's how we go through the process. 9/8*

The standard procedure for assessing a SME loan application follows more or less the same path and the emphasis is on three elements; financials, security, and character.

When an existing client approaches his/her bank manager for a loan proposal, the business manager begins the process of assessment by conducting an interview session with the client to determine things, such as what s/he needs, the amount, purpose, and duration of the loan as well as to explain to the client the information he/she needs to supply. Inputs from previously conducted interviews and information collected from other sources as part of assessing previous loan applications are also used. Interviewees 12 and 8, respectively, had this to say about this step:

*An existing customer will generally have a trend of their account within our own systems. They obviously tell us what they're wanting to do in that particular point in time then we'll ask for updated financial information. 5/12*

*You go through the process; these guys come to us or referred, whatever, and I have the initial discussions with them and find out what they're doing. Now, where I'm doing, there's scoping to make sure that it's a proposal (1) that we're interested in and (2) that we can do. And there's non-target industries out there that we're pretty careful about who we deal with. We don't want all the hotels. We don't want all the cafes in the place. We've probably got enough exposure to those like most banks, so there is some non-target areas. So we have those discussions and we just... once I've established that (1) that we have an interest on we should take it further that's when I've got a sort of a format on what I require to take it [to the] next step. 19-20/8*

## V.4.1 The lending criteria

### V.4.1.1 Financials:

The financials are pivotal as the objective is to assess the debt serviceability of the business in line with banks being cash flow-based lenders as explained by interviewee 12

*I'm not a security lender. Finance companies are security lenders, and all those asset, you know second tier lenders, they're all basically what we call asset lenders. We're based off cash flow. 10/12*

The financials might include an updated balance sheet, budget and cash flow forecasts, particularly in the case of medium sized enterprises, a debtors and creditors schedule on an age basis and other documents, as neatly explained by Interviewee 21 who provides some explanation as to why these documents are required.

*So, typically, what we would like to get off a customer is their financials. That's both their balance sheet and their profit and loss, then we'd like to get what we call a statement of position off them and then we'd like to get a cash flow forecast. And then in me ... just so we can get a wee bit more understanding and substance around their liquidity, we might ask for a debtors or creditors schedule on an age ... trial basis and that way we can have a look at the company's historical performance – are they looking out the back window? - and then with the cash flow forecast we can look out the front window; then we can look to mitigating the issues they might have going forward. 1/21*

Banks have their in-house systems or computer programs for business managers and/or their analysts that they use to extract information

from the financial data supplied by the client, to distil and construct what they need in terms of ratios such as earnings before interest and taxes (EBIT) etc, and to perform some more sophisticated operations, such as sensitivity analysis, particularly in the case of bigger businesses. The aim of this type of analysis is explained by interviewee 19.

*So we allow a margin line. For example, we'll generally look at a margin above the current interest rates, so building a buffer to prove that you know if there is some, if an interest rate moves they can still afford the loan.4-5/19*

Interviewee 14 explained more about the in-house system and its use, saying:

*Then if it's borrowing over five hundred thousand, we put their financials into a system that's called XXX at bank name. It's called different things. Every bank calls it differently. It's called XXX at bank name and what that does is we just put in all their profit and loss and balance sheet and it spits out a whole lot of ratios, their quick ratio, current ratio – all just quite basic sort of stuff there, changing their sales levels. They're changing their gross profit margin and that gets, if it warrants it then, if the borrowings are enough we use that and then that talks to our rating system, and it puts certain ratios into the rating system which it helps to ... the rating. 7/14*

Overall then, what the bank/business manager wants to establish is represented by the comments of interviewee 12:

*Whether I lend or not is against my judgment depending on [whether I] am satisfied with the cash being generated from the business as sustainable; is (1) sustainable and (2) is enough to pay back. 13/12*

Also as part of the financials, business managers have access to specialists within the bank to help them with other aspects of business banking that are beyond their expertise, especially when the level of complexity involved is too high. Elaborating more on this issue, interviewee 23 said:

*The other thing we'd use is specialists within the bank. Obviously I don't handle all aspects of business banking; we've got specialists for international, credit card, card eftpos facilities, and transactional specialists if they're complex transactional structure – a lot of accounts for one business. So, just involving bank specialists as well, which are often brought into an interview situation where there would be myself plus the specialists involved. Yeah. And even interest rate specialist and that type of thing, if somebody's got a large debt exposure, just trying to assist them with how they should structure their interest rates – fixed or floating.9/23*

#### **V.4.1.2 Security:**

The second key element, security, covers things like the collateral pledged by the relationship managed SME client; how is it valued, how much is required for the new loan proposal and at what terms? It is predominately a tangible type of security, such as residential and commercial properties of the owner/manager(s) and some of the business assets, such as printing machinery in the case of a printing firm for example.

*We're predominantly landed security. Land? Land, yep. So, we're talking about residential or commercial. They're the two predominant ones we deal with. We can deal with debenture or they're called general security deed. You know, so it's a floating*



*charge on the assets of the business. But they're few and far between. There's quite a few constraints that come along with that in terms of, you know, suitable equity, suitable projections showing good profit, good history account conduct; there's quite a huge more belts and braces if you like for debenture lend. 12/8*

A few interviewees spoke about how intangible assets are also used, but much less often. Intangibles appear to only be used as a supporting security, and tend to be used with bigger businesses and higher lending amounts.

The majority of interviewees expressed the view that, in business banking, security is a key requirement. There were very few instances where unsecured lending was possible and then only partially. An example is related by interviewee 2.

*If the security side is not that strong, but the business owner has a lot of experience in what he's doing and the business is going well, it's a very profitable business, we can **consider** unsecured lending. 3/2*

However, banks won't lend against security alone if loan serviceability is missing, as stated by interviewee 12.

*We don't do it. Generally in business we're not asset lenders apart from if someone wants to, say for example, buy a particular truck for their business; whilst we call that asset-finance lending, whether we lend or whether we don't is against their ability to repay, or their assessed ability to repay.*

***So it's not against the asset per se?***

*No. If you walked in here with a house worth five hundred thousand, had no liabilities, didn't owe anyone any money and you said to me, "I want to borrow three hundred thousand"*

*which is within our basically 80%, so if he said I want to borrow three hundred thousand, I would then ask you well, how are you going to pay that back? 10/12*

Another reason for not lending against security alone is reputational for the bank. Only a few interviewees touched on this point, and interviewee 14 explained this further saying:

*If the cash flow doesn't stack up, we don't care how much security we've got because it's costly to go down the track of selling securities and things. I mean although we get that cost back but it's also reputational risk as well. I mean that person in the meantime is going to be slagging off [bank name]. It's not a good look for us to be mortgagee selling houses. 8/14*

This is because banks aren't asset lenders like finance companies.

Finally, security is used as an input, along with the financials and character related information, into the scoring/scoring system toward the overall decision about the loan, its price, and the conditions that may have to be attached to it. This exercise is performed by way of scaling the security to get a grade as further explained by interviewees 14 and 8 respectively.

*And then the security side of it can be A through to J depending on A, sort of lots of security and J is no security at all. And so the average customer is probably between twelve and eighteen and let's say most people would be a D which means that it's just sec, fully secured but only just, and then what we do, unless it's a housing type, secured by housing, in which case they will go with a housing loan. That rating helps us determine what interest rate to charge, so the better rating they are, the lower the margin that we'll charge. 7/14*

*We take security and we scale it so that gives a number at the end. So you know what you can lend up to. In the serviceability you know what the proposed debt's going to be and the terms that may vary according to the security - as explained by interviewee. 32/8*

#### **V.4.1.3 Character**

“Character is paramount”; such was character unanimously described by all the interviewees in one way or another. In fact, character is so important that it could tip over the whole application as per the following hypothetical example supplied by interviewee 6:

*If someone was a real bad bugger, he's bad character, doesn't matter how good the security is, you say, 'bugger off'. 6/6*

Reflective of this consensus, interviewees 17 and 19 respectively, justified this importance as follows:

*Because if we don't meet the client then how do we understand what they're like, what they do, how they do it, and it's not until you actually meet someone and talk to them that you actually can get more of an understanding as to what they do. 31/17*

*You can have somebody who on paper has the income but character – they may have a bad credit record or there may be some other aspects of them personally that indicate that even though they have the income, you're gonna have problems with them meeting loan repayments. 6/19*

This part of the assessment covers two types of data which could be divided and labelled as hard data and soft data. Hard data covers aspects such number of years in business, numbers of years with the bank, and performing credit checks via VedaAdvantage, as explained by interviewee 8 who added:

*Making sure the credit checks don't come up with anything too adverse. 9/8*

Soft data assessment, however, is done mostly through interviews conducted by the business manager. Some of these interview sessions are *strategically* conducted at the client's working premises, or in their natural business settings. On one hand, this allows the business manager, among other things, to look around, meet the employees, ask questions to obtain/assess information in order to gain an understanding about the client's internal information and reporting systems as part of the management risk assessment, because, as interviewee 5 explained:

*When you ask those questions some people answer, "Oh, I don't know, my accountant deals with that." You know that they don't have a good understanding. They might understand the business but perhaps not the financial management side of it. So, you can see how reliant they are on other parties, which is fine if they've got systems in place that back that up. 7-8/5*

Business managers develop a set of questions that they ask their SME clients. Direct and indirect questions are used tactically, giving business managers some hints/indications as to their clients' level of understanding, commitment and knowledge, etc, as summarised by interviewee 5:

*You ask them certain questions about how the business is running and if they have that information at their fingertips and they know that stuff then you can see that they're really on top of their game then you know that they're in a good space to be running that on-going, so it's a little bit around have they been*

*running the business and has it been successful, therefore they must have some skills in that area that they've managed to do that. 7/5*

This way, valuable and often intangible information is accessed, assessed, and recorded by the business manager as part of the client's profile. On the other hand, it is an opportunity for the client to explain themselves and their business more fully, saying things like:

*This is what I'm doing; this is making how much money a year, etc. 5/2*

As narrated by interviewee 2.

Furthermore, and as part of soft data assessment, the small business owner/manager is also assessed on his/her understanding and capabilities about the financial side of the business. This is important as one interviewee 12 explained:

*Because they need to know, if I ask a customer what's his gross profitability, and if he can't tell me or he doesn't know what influences it, then how's he going to be successful because the financial part of it is one thing; the actual management of the business is another thing. So, you can't sort of look at one in isolation. So, we'd ask them basically, well how do they control the day to day management of the business; what reporting systems do they use? How do they do it? 7/12*

Finally, all the information about character, hard and soft, is then used to work out a risk level based on the character which will then be used with the financials and security to decide about the loan application, pricing, and conditions of the loan if successful.

In addition to the standard procedure outlined so far, with medium sized enterprises, i.e. big loans such as over half a million dollars in the case of ANZ bank, the relationship manager also writes a report to build a more comprehensive profile about the business. This report seems to be judged as 'more subjective' by some managers.

Interviewee 14 elaborates more on this point saying:

*We also do quite an extensive write up in terms of covering why they need the money which is an important part of it. Does what they're doing fit with what the actual nature of the business is? So if it was a car yard wanting to buy a coffee shop then that wouldn't be a very good business fit sort of thing, making sure that we've got our return on equity right, looking at the debt servicing side of things, so we do a debt servicing spread sheet based on what their EBIT coverage is and things, and their payment cover. So, we take their earnings, depending on the business, earnings before interest and tax, and sometimes we'll add back depreciation depending on the nature of the business and then see how that covers their interest payments and their principal interest payments.8/14*

Once all the information related to the three criteria of financials, security and character are gathered, they are then processed through the scoring system to make a decision about the loan application, taking into account the written report by the relationship manager in the case of big loans. Interviewee 5 explained this:

*Ok, we have an automatic – what do you call it – a scoring tool that you input the information into and it assesses whether the deal meets the criteria or not. So, that's one tool we use. And we have another one that just, we call it a judgmental pad, so one is the tool makes the decision around whether this is the deal that ticks all the boxes for us. And the other one is a judgmental discretion that we have a big fat policy book with*

*lots of rules in it which I'm meant to know and I have a discretion to make decisions based on if the application meets the policy and meets the certain criteria. I can then say, "Yeah, it's a deal. We will do it." And if it doesn't meet policy or if it's outside my discretion then I send it up to the next level of discretion making to make a decision.*5/5

The next section deals with the different outcomes from the process described above.

#### **V.4.2 Possible outcomes from processing SMEs loan applications:**

There are three possible outcomes from the decision-scoring tool. The first one would be a 'yes', in which case a letter of conditional offer is sent to the client outlining things such as covenants, security the bank will take, and interest rate.

The second outcome could be a 'no' verdict, in which case two scenarios occur. If the application falls within the business manager's discretionary limit and s/he sees no merits in using his discretion to override the tool's decision, then that will be the end of it. If however, the application falls within his discretionary limit and he can mitigate the 'no' reasons, then he can override the tool's decision and turn it into a 'yes'<sup>27</sup>.

---

<sup>27</sup> Though banks in New Zealand were relatively late in adopting credit scoring (Ministry of Economic Development, 2003a), the interviews revealed that the banks are progressively introducing it into the SME market, apparently at different stages. The reasons for introducing it are because of changes to the reserve bank and international reporting 'Basel II'. However, from some junior and some senior manager perspectives, the use of credit scoring seems to bring with it

There are different discretionary levels for different products and services and it is decided upon a matrix with certain criteria as components. Interviewee 5 explained these components and the dynamics around the discretion issue saying:

*It's got lots of criteria around it so it's scaled around the quality of customer and that's based on things like how long they've banked with us, how stable their profit's been; how good their account conduct is; if it's an existing customer; those sorts of things. That will give us sort of a risk profile around that customer and we also look at what security they're offering as well, and the combination of those two things determine what discretion I have but I have different discretions to different things. I have a big discretion for home loans and then I have a different discretion level for business loans and a different one for credit cards or foreign trade limits or depending on what they're doing. Ok, so it's based on the product that they want on one side and the quality of the customer and the quality of the security on the other. So, it's a kind of a table.5-6/5*

The discretion levels are also affected by the general conditions of the economy.

The third possible outcome is when the application falls outside the business manager's discretionary limit. The loan application gets transferred up to the next level where there is higher discretionary authority to make a decision. Because the processed application is saved on a central database, the assessors at the next level up can access it. The business manager also writes a referral report saying something like:

---

an unwanted aspect; it is taking away some decision making from the business managers and giving it to the credit score controllers/makers.



*Though the tool hasn't approved it why I still think it's a good deal.*<sup>5/6</sup>.

Based on the referral report and the application, a decision will be made. However, it seems that when an application gets transferred up to the next discretion level, the assessment is more or less limited to the two factors - financials and security. The following quote from a small business manager explains that further illustrating the issue with two examples.

*If I send it to a credit centre, they don't know much about that one<sup>28</sup>, so they will be assessing mainly on those two<sup>29</sup>. So when it goes to a credit centre they almost take that personal factor out of the equation. Whereas I'll have people for example that'll walk in here and ask me to borrow a hundred thousand for a week, right? And I will give it to them. The next customer that walks in and asks for a hundred thousand, I won't. But that's where the personal factor comes in to it. So you do have some ability to influence whether you do or whether you don't purely against the personal factor. Do I trust this person? Do I not? Am I comfortable? Am I not? So, there are certain customers that I would trust within our own parameters of course but I can give them probably a bit more leeway than other customers. 11/12*

All interviewees were of the opinion that often, and with all declined loan applications, a 'no' answer is the start of another process of the business manager explaining to the SME owner/manager why the application was declined, offering alternatives and possible courses to follow to help the client, as interviewee 9 explained further:

---

<sup>28</sup>Character

<sup>29</sup>Financials and security

*If it is an existing client and you know the situation deteriorated and their grade has gone down, what that means is that we're going to start requesting more information and we're going to try and manage them back up to a point where we're happy with it again. Because it comes down to a certain grade doesn't mean "right you're gone", it says "okay look, there are some issues here, we need to do something" and that is perhaps you need to get your accountant involved. "We need some more regular information because there are things within your business you need to improve," and then we sort of review on an on-going basis and try and get them back to an acceptable level. 9/9*

#### **V.4.3 The non-segregation of loan underwriting to**

##### **SMEs:**

To test whether banks and their bank managers segregate the contributions and effects of each of the three agreed-on criteria of lending - financials, security, and character - on the final decision for a loan application, the interviewees were presented with a thought experiment as a hypothetical lending scenario. This lending scenario was presented as follows:

*Say I'm an existing customer and say the relationship started here, way back here for example, and I borrowed money here and paid it back here and came at this point to borrow some money and you asked me for an update financial statements, some security and all that. I provided everything; I got to a point where you said, 'Okay, yep, I'm giving you the loan,' and everything decided; in fact, has been signed including the conditions, the price, all that. If you were to think retrospectively at that point with that particular customer, and with that particular loan application, would you be able to say, 'Well, this loan application was okayed with say, sixty per cent was based on the financial statements, thirty based on the assets, and ten say, based on the character, relationship banking.' I don't mean necessarily 60-30-10 but just some weights. Could you do that? Do you do that?*

The answer was unanimously negative. Typical answers were along the lines of interviewees, respectively 9 and 13:

*It's probably more in personal banking where they have sort of a formula, a sort of tick box formula lending where in the business banking; no it's not quite like that because I suppose businesses are quite varied and quite different but rural banking maybe you could, like dairy farming, you know for example there is, you've got certain size farm, certain production, certain payout and then that way you can sort of do fairly much a formula type lending to a large degree. In business you've got quite different - you know - your retailer to your manufacturer, to your property developer; it's all quite different so it's very difficult to actually put that into a standard...7/9*

*The bank's got criteria for these two [financials and security]. So, the numbers may look like that. It may be like that but we don't do it actually, write in; we don't do it like that, no. Well, probably not because we've got... no. If you looked at a file it wouldn't be spelt out like that, no. 11/13*

Different justifications were provided as to why the loan segregation doesn't hold. One justification was that of interviewee 9 above - business being different. Other rationalisations included clients being different even within the same sector, projects being dissimilar, past experiences vary from one customer to another. Interviewee 14 provided an example on the last justification:

*By way of example there is a certain customer I have through say, five years ago. The bank lent him some money, which was very risky at the time, and he exceeded all expectations and did really well. He's at the point where if I take something to our credit to get approved, they will stretch the rules a lot further for him than they would potentially more than they would for a new customer. And then there's other customers who things turn to custard so if something looks like really good on paper but*

*it's the customer who's managed to muck something up for then potentially we won't back them so that relationship part can. And then there might be some cases where I guess an ok customer is buying a good business, good financial statements and good assets, so they might be more evenly weighted.13/14.*

This finding of non-lending segregation of loan underwriting confirms Berger and Udell (2006) point on the contribution of each of the lending technologies to the final decision about a loan application. This research provided a first empirical exercise to check/test for that assertion. Furthermore, and most importantly, this study has provided an explanation as to why loan underwriting segregation is hard to achieve. Relationship banking is an umbrella model within which you can't separate the contributions of each technology for the overall decision. Banks do not yet have systems in place to allow them to do so.

A research implication here is that to investigate the contributions (and benefits) of relationship banking to the banks performance can only be studied through the use of proxies such as those used by Bharath et al. (2007), Ergungor (2005), and Puri et al. (2011), validating their research approaches. A direct approach to this investigation would be a case study approach such as interviews, which would be the only method suitable to both investigate directly and separate the contributions of relationship banking from the input by credit scoring and other lending technologies. This gives further

validation to the research approach/method used here to investigate the relationship banking benefits accruing to banks and the processes of securing them.

From the discussions about the lending approach and criteria used by banks to assess SMEs' loan applications, four implications follow:

One, there is a high level of congruence among/by banks in their lending approach and procedure to their SME clients; from the use of lending criteria to the non-segregation of loan underwriting. However, when it comes to the three criteria of lending – financials, security, and character - this congruence is slightly different from what is often discussed and emphasised in primary text books about lending (Bass & Rozario, 2011; Greenbaum & Thakor, 2007; Koch & MacDonald, 2009). These references emphasise what is called the 5 Cs<sup>30</sup> of lending as illustrated by Koch and MacDonald (2009) stating “when evaluating loans, bankers cite the 5 Cs of credit: character, capital, capacity, conditions, and collateral” (p. 677). There were even a few instances where interviewees had never heard of the 5 Cs concepts, even after I introduced it to them. However, the two Cs not explicitly mentioned by the interviewees are still embedded by bank managers in their decision making. For example, conditions - being

---

<sup>30</sup> Sometimes referred to as 5 P's (People, purpose, payment, protection, and perspective) or CCCPARTS (Character, capability, capacity, purpose, amount, repayment, terms, and security).

the fourth C- because bank managers assess financials, security, and character (FSC) as well as all other variables that (might) affect those three elements. Doing that means taking into consideration the overall conditions which is exactly what is meant by conditions under the 5 Cs formula of lending. This might mean that, at least in the New Zealand context, another variant of the 5 Cs is the FSC or the 3 Cs.

Two, because of the high level of congruence among the five major bank brands, there is a considerable amount of uniformity between them in a lot of the practices as they relate to SMEs. Consequently, bank managers won't need much retraining if they were to move from one bank to another. This would lead to a high level of portability of bank managers between banks which may explain the high turnover of bank managers referred to in the literature (Gan, Cohen, Clemes, & Chong, 2006). In fact, bank managers would be much encouraged to move banks to enhance their careers for example. While this might be good for bank managers and banks, it is the source of frustration for their SME clients. It affects the flow of relationship banking and SME clients have to start new relationships with new bank managers.

Three, from addressing the issue of how banks assess loan applications from their SME clients (above), it becomes apparent that character is a key element of relationship banking. The assessment of

character by the bank manager is based on assessing the business owner/manager's management ability, business understanding, integrity, and honesty. Furthermore, a point of differentiation between micro-to-small businesses and small-to-medium businesses is that the former are managed via call centres through credit scoring procedures. This means that those smaller businesses will not receive relationship banking services. However, a complete and proper assessment of 'character' is only possible when it is done by a bank manager through relationship banking built with and around the SME owner/manager. This is a likely indication as to why smaller businesses face a supply-side financing gap and/or a higher risk premium than is appropriate for their actual risk level. This can be added to the list of reasons given for the financing gap (OECD, 2006) with responsibility attached to banks. Furthermore, this suggests a need for alternative method(s) of character assessment other than the current computer-based credit scoring, if banks are going to improve the flow of funds to the smaller end of the business market.

A future study to statistically test this proposition could use the following proposed experiment. First, identify a sample of similar small businesses that under normal circumstances would not qualify for a proper character assessment because they are managed online. The second step is to divide these businesses into two groups. When

the first group of businesses applies for a loan, all else being equal, they would be assessed on character the same way a relationship managed client would be. The businesses from the other group, the control group, would continue to be assessed the same way online businesses are assessed whenever they apply for a loan. Finally, a statistical analysis of the results will shed some light on the validity of the above proposition about the role of character assessment in the supply side finance gap.

Finally, what follows is a possible explanation as to why character is viewed as paramount among the three elements of lending that are emphasised by banks in their assessment of their SMEs clients. Character can be divided into two parts, the character's capability and his trustworthiness. In theory, we can say that the character's trustworthiness is the only element that is expected to always go up in value as time passes whereas the other two elements – financials and security - can and do go up and down depending on circumstances that are outside the control of the SME owner/manager. An example of this was the outcome of the last financial crisis when almost every house and/or work premises used as collateral decreased in value. The crisis was exogenous and the SME owner/manager had no input in it, yet it affected the value of his collateral. However, the character is endogenous in that being trustworthy, for example, requires only the



SME owner/manger's freewill, is completely within their scope of control, and depends only on them and their own decisions. In practice however, the character's trustworthiness do go up and down. This indeed makes character different from the other two (or four) criteria of lending.

### **V.5 What is relationship banking to the five major bank brands in New Zealand?**

When all of the interviewees were asked for a definition of relationship banking, no formal/precise definition was provided. All interviewees tended to define relationship banking by what it does rather than by what it is. An example of this was from interviewee 2 whose first comment was this:

*I guess my understanding is it's just to be there as an individual to know your customers; to provide a personalised service that the customer needs. It's trying to create that atmosphere; when the customer needs something from the bank, they are not dealing with the bank, they're dealing with people. 6/2*

Furthermore, the interviewees seemed to drive/acquire their definitions of relationship banking on the job. This might be due to the banks not supplying their managers with a formal definition, as explained by interviewee 7 who said:

*There's no word that we get told, I mean it's just your own personal interpretation of it. 13/7*

Notwithstanding those issues, when the interviewees' comments about relationship banking were placed side by side, and contrasted, a working definition started to emerge resulting in a consensus among all interviewees on what relationship banking is about. This definition revolved around four main points:

1. Business managers are the single point of contact and a one-stop-shop for all of the SME banking dealings and requirements. Reflective of the unanimity of interviewees on this point, interviewees 17 and 22, respectively, said

*Well to me it's giving the customer the ability to, for me to be the one stop-shop. So I am the Bank [name]... if there's things that I can't find out for a client or tell them immediately I have to find out. That's my job. Um, so, so they shouldn't have to go running to different departments to do different things. They should just come to me straight off and I should be able to give them all the answers that they need, or find out all the answers that they need. 7/17*

*I suppose it's being a bit like a 'one-stop-shop for any banking type facilities'. We've got everything from borrowing, deposit funds, insurance that sort of stuff, so banking is quite a lot wider than what it used to be. But basically, being a one-stop-shop for all that sort of thing where a client would only think if they wanted something, 'I'll talk to [John] first.' 9/22*

2. These business managers are then directed and expected to learn about their relationship-managed SME clients and their businesses. This learning and understanding is actively pursued by business managers about each and every one of their SMEs in their

individual portfolios and the individual owner/manager. This point is represented by interviewees 21 and 14 respectively

*It must start with us understanding the customers' needs. You know, customers I think, they say to us, "Look, know me, understand me, know what makes me tick, know what turns me on." You know, some customers are very fee-averse; some aren't. Some are very ... conscious; some aren't. Some are very particular that they like to be pampered; some aren't. So it's about understanding the needs, the entire needs of a customer, understanding their business and their trade cycle, understanding what influences the world markets have on their business. 8/21*

*[Its] getting to know your customers, their ways of doing business because everyone has different ways of doing business.... So there are some customers who yeah, I won't call them unless they call me because that's how; they don't want to be bothered by the bank. Give me the money, let me do my business and bugger off and leave me, and other people will be like, look I want you to show me the love. I want you to come and see me at least once a month. I want to know what's happening in the economy. I want you to come in and help me out with my business. I think that's what relationship banking is, is tailor-making how you deal with your customers according to their personalities and their businesses and things. 15/14*

However, this tailored understanding of the SMEs and their owners/managers isn't required to be exhaustive, as explained by interviewee 12.

*As part of the relationship we've actually got to understand what their business is, we don't have to know it inside out, but I've actually got to know what they actually do. 35/12*

3. The tailored understanding is then used to tailor manage the SME and tailor the bank's offers to the SME, not just in terms of what,

but also how and when. This point was well captured by interviewee 20.

*Having the relationship manager who can actually, you know, get to know a customer and what's happening in their business. You know, they can then start to introduce a wider range of products to them, rather than that just being driven centrally using marketing analytics and data. Actually having someone who knows that customer, you can offer – put a much more relevant offer in front of a customer. You know, it's basically a one-on-one offer and it's also the timing of that offer. So, you know, the relationship manager should know what's going on with their customers, and therefore when's the right time for the right offer. So it's a much more targeted way of marketing our products and services than say, you know, direct mail for example or other forms. 3/20*

4. Finally, relationship banking is not limited to an understanding and assessment of the intangible side of the SME and its owner only. It is, as succinctly summarised by interviewee 23,

*So, relationship banking is the whole scenario. 10/23*

Relationship banking includes the use of and assessment of financials, credit scoring and collateral. It is viewed as an overall model within which all financials, security and character assessment are all used.

Two more issues emerged about the workings of this relationship banking that were pointed out by all interviewees. First, interviewees spoke about the relationship being with the SME owner/manager, and it is built with and around him/her. Interviewees 23 and 22, respectively, explained this saying:

*The relationship firstly is with the owner. And then because often if a, for example, business is sold, often we would lose their business because the person buying it might deal with another bank. So, your relationship is with the owner directly but that's probably a higher weighting on the owner than the business itself as far as the relationship. Obviously if it's a good business you'd want to try and continue banking it - if it was coming to a sale arrangement - but that's a lot of cases where we'd lose that relationship with that business through the sale of the business.*

***Because you're going to start all over again with the new...***

*With the new person with different characteristics and background etc. And as I said, they may already have a banking relationship with another bank. So, in answer to your question I think the relationship is with the owner. 20/23*

*With the owner. Yeah. So the person who's making the decision.... Oh, yeah, absolutely. I can't really have a relationship with the business as such because it's small businesses, the people are the business, as opposed to a big corporate where you've got the people running it - you have a relationship with them but they might not even own the business. They make all the decisions but they might only be the finance director or the managing director, they might have a small shareholding, but they might have none but they're the ones who make the decisions. 11-2/22*

Secondly, however, interviewees perceived SME owners/managers as having a relationship banking bond with both the bank and the business manager. This was summarised by interviewee 7:

*It's definitely both yeah.*

***How much weight can you [put on each one of them]?***

*It actually varies on how involved the business banker is with a customer and the extent of the relationship. And how they go about building the relationship, there are clients that will change banks because their business banker has changed. And there's client's that won't change banks because they like [bank name] in their relationship, will always sit with [bank name]*

*because their relationship is with the brand. We know it through our surveying clients if we actually can get an understanding of what that may be in regards to each relationship person. 16/7*

There was a consensus among interviewees about the very small number of SME owners/managers who would follow their business managers when s/he changes banks and/branches. Interviewee 3's example is reflective of the consensus.

*I have one customer that says 'if you're not there I will remove my accounts'. So, then he has a relationship with me, not the bank. But if I go tomorrow and someone else replaces me, the other percentage will be with the bank.15/3*

The flip side of business manager turnover, however, from the SME owner/managers' perspective, is that they have to restart part of that relationship with the new business manager from scratch. Interviewees reported this as being a source of lot of complainants from their SME clients. Interviewee 22 explained this further.

*That if they wanted something the first place they'd think of is, 'Oh yeah, I'll ring [bank name] or ring Steve,' or whatever. But I guess the problem is, bank staff tends to change quite a lot and it's the one thing customers don't like. **Yeah, because they will have to start again.** Start all over again, and so the relationship, while it's with one person, it's gotta be built across the organisation really, so that if they've got lots of specialists that we can bring in that they can deal with so they don't have necessary relationships specifically with one person, or they do see that first point of contact with one person but they have someone in international or merchant services or something like that, that does those specific things for them. So the relationship's broader than one person, and that will survive if people change, but if one person does everything and every two or three years they move on, and their business*

*carries on for 20 years they're gonna get really sick of that. And a lot of them do, a lot of customers do.... I've had one client that followed me from branch to branch to branch. But I would say, I certainly wouldn't encourage that. I wouldn't think that would happen that often now. Most people seem to have got used to the fact that managers change and so, while it's disappointing, they live with it and move on and they know they've gotta start all over again. 8-10/22*

The working definition of relationship banking distilled from the interviews departs from the established definitions, such as those of Boot (2000) and Berger and Udell (2003) reported earlier (in the literature review chapter) on a number of counts.

First, it is true that relationship banking allows the bank, through its business managers, (among other things) to collect and use soft data in the decision making about a loan application which would then qualify it as a lending technology, using Berger and Udell's (2003) definition of lending technology. However, the relationship is also the melting-pot where *heterogonous* inputs/information and sources of information from all other technologies are used together, side by side and 'none in isolation' to make a *homogenous*, overall and final decision. This makes relationship banking more of an all-encompassing umbrella under which other technologies are used. In other words, banks use relationship banking not just as a lending technology on equal terms just as they would use other lending technologies such as credit scoring, when dealing with their SME

clients. Rather, banks make use of relationship banking as an overall *model* within which other technologies are used to bank their SME clients.

Secondly, while Boot's definition (2000) centres around two critical points, one being the proprietary information (as has also been established by this study) and the other being the evaluation of the profitability of investments through multiple interactions with the client over time and/or across products. That definition of 'relationship' could also apply to small businesses managed online. The three conditions that Boot (2000) enumerates for relationship banking to exist are all present in the case of those small business. The three conditions are:

- i. "The intermediary gathers information beyond readily available public information;
- ii. Information gathering takes place over time through multiple interactions with the borrower, often through the provision of multiple financial services;
- iii. The information remains confidential (proprietary)" (p. 10).

However, this current study found that the online management model cannot be qualified as a relationship banking model using the



interviewees' definition. With the online model there is no designated and dedicated business manager to each specific SME, the character assessment performed by the business manager as explained earlier is absent - including the assessment of soft data related to the SME owner/manager's business understanding and capability, and trustworthiness; all of which can be deduced via a dedicated business manager by way of, for example, having face-to-face meetings with the SME owner/managers, and/or visiting their working premises.

Finally, the often quoted definitions of relationship banking in studies about relationship banking, such as that of Boot (2000), give the impression that relationship banking is actually between two organisations, i.e. a bank and a business. However, this study's findings show that relationship banking with SMEs is a relationship between persons rather than organisations only. The persons involved being the owner/manager from the SME side and the business manager from the bank side. Though from the SME side the relationship is concentrated with the SME owner/manager, from the bank's side it might be more accurate to talk about relationship banking as being mediated through the business manager. In that sense, when the business manager moves branches/banks, the relationship with his clients will be affected, but not to the same extent as when the SME owner/manager changes.

Further, banks could strategically and intentionally use relationship banking as a strategic tool of differentiation from other banks and financial intermediaries especially when other providers offer the same financial products.

- 1- Unlike accountants and lawyers, business managers do not charge per hour of consultation.
- 2- Banking products and services are fairly similar among banks, and giving recommendations is a way for banks to differentiate themselves, help their SME clients, and retain and gain customers.
- 3- From dealing with SMEs across sectors, some of which are similar to the small business seeking recommendations, the business manager develops skills and a knowledge base that would be useful for the small business.

## **Conclusion**

This chapter began the analysis part of the thesis reporting on how banks split their activities and define SMEs using qualitative and quantitative criteria. The chapter elaborated on the banks' business banking relationship model(s) taxonomy used by banks, detailed banks' lending approaches and criteria used when lending to relationship managed SME clients, and finally reported on what

relationship banking is to banks. The next chapter deals with relationship banking benefits accruing to banks and how banks secure them.

## **VI. Analysis and discussion –II–: Advantages of the relationship banking model**

### **Introduction**

This chapter is pivotal to the thesis and is where the research findings concerning the different relationship banking benefits to banks and how they are secured are reported in detail with much analysis, discussion, and consideration of implications for both the academic literature and the banking industry.

The chapter is structured around first reporting the identified benefit, and the process of securing that benefit by answering the questions around what information banks acquire, how they obtain it and how they use it. Then, a contrast with some of the relevant literature is carried out, and implications put forward. This structure has been followed with all of the 14 benefits, each in a separate section. Finally, the chapter concludes with discussing two taxonomies/classifications of benefits developed from approaching all the benefits discussed in this chapter all together in a meta-analysis, and the benefits of these taxonomies/classifications to banks are reported.

## VI.1 Cross-selling:

Cross-selling was the first relationship banking benefit to be explicitly raised, unprompted, by all interviewees.

Banks supply more than just loans to their SME customers, as interviewee 4 stated:

*Banks aren't just about lending. We make our money through selling our services; it's a service industry.... So we sell insurance policies. We sell overseas trade. We sell mortgages. We sell um – we sell dreams. We sell leases ah, for vehicles.*  
39/4

The above quote has elements consistent with the standard definition of cross-selling. Cross-selling is defined as a strategy for the bank to sell/push new products and services to its current clients based on their past purchases. The objective is to widen the small business's reliance on its bank and decrease the risk/likelihood of the client changing banks (Kamakura, Wedel, de Rosa, & Mazzon, 2003).

Relationship banking was considered a way to facilitate cross-selling in a general process of three steps, which can be deduced from the following three quotes reflective of all the interviewees' different perspectives:

*You can sell more things as a human being than you can as a computer or as a, as a straight sales person. You get to know the person. You get to know the things that drive them. You get*

*to know a lot of information about people. Therefore you get more opportunities to sell them things. 39/4*

*It is providing a complete financial solution to the business owner so that we cover their personal banking, their business banking, insurances, any trade foreign exchange needs, anything like that; any of those financial needs that they might have. But because it's done on a relationship model it's an on-going relationship and I think that's what makes it different because you develop over time an understanding of the individual and how they operate and what their needs and so you're able to sort of really tailor things to suit them, and to spot gaps, things that they haven't perhaps considered or whatever. You can be quite proactive around the relationship. 16/5*

*So I guess from the sales perspective, you know, having the relationship manager who can actually, you know, get to know a customer and what's happening in their business. You know, they can then start to introduce a wider range of products to them, rather than that just being driven centrally using marketing analytics and data. Actually having someone who knows that customer, you can offer – put a much more relevant offer in front of a customer. You know, it's basically a one-on-one offer and it's also the timing of that offer. So, you know, the relationship manager should know what's going on with their customers, and therefore when's the right time for the right offer. So it's a much more targeted way of marketing our products and services than say, you know, direct mail for example or other forms. In saying that, you know, we do use that as well because even though we do relationship manage, we've got a large number of customers and we have to support the relationship management marketing activity with some of the more mass marketing activity. 3/20*

This general process, consisting of three steps begins with the opportunity for the bank manager to properly understand and evaluate the SME and its owner/manager. The second step allows the bank manager to identify the SME needs in terms of banking products and services through this understanding and evaluation process facilitated

by the situated context/relationship. The final step is to present/offer/market those products and services relevant to the SME's needs and at the right time as workable solutions to the SME and its owner/manager's needs.

Therefore it is through relationship banking that the business manager gathers all of the relevant information, hard and soft, about the SME owner/manager, his/her business and assesses it. This is possible because the relationship allows the business manager to act as an *insider* which is not possible in a non-relationship banking setting. In addition to this, the business manager, with his knowledge of bank policies and products and services the bank can offer, is able to identify the SME needs and the way the bank's products and services can meet them. This illustrates how relationship banking, rather than being a lending technology as posited by Berger and Udell (2006), is an overarching model within which bank technologies, such as credit scoring and financial statements based lending, can be introduced and, used as discussed in section V.5 above.

A further five issues emerged from the interviewees relating to the benefit of cross-selling, and are as follows:

- The cross-selling benefit is not limited to the SME and its owner/manager's needs, but extends to include his immediate

family as well. This highlights the benefit for banks in defining SMEs as groups, which include the SME, its owner/manager, his immediate family rather than solely the business as a discrete physical entity as it is commonly defined. This point has been discussed in the analysis section on SME definition. Therefore the banks' definition of SME widens the opportunities for the bank to meet the needs of the group.

- A point related to the above is that relationship banking informs not only *which* products and services to offer next but also *how* to offer them. Elaborating on the issues surrounding how this works, interviewee 5 said:

*I think part of that relationship perhaps is that you get an understanding of the whole picture which means that you can identify the things that are important to the customer and the things that they don't like so that you can structure it in a way that you lessen the things they don't like. You identify that a guarantee from this party is really not their preferred option. If there's a way that you can present it so that we don't need to include that party but to mitigate that we can do it another way. So, you can use that information of understanding the whole picture in structuring things in a way that they meet both the bank's requirements in terms of making the risk comfortable and the customer's requirements around how they want to structure it and how they want to include whatever and depending on what their plans are what is the best structure in understanding all that. 24/5*

So the bank manager is able to tailor the bank's offers to the SME owner/manager and their business needs, thereby minimising the chances of "weaken[ing] the firm's relationship with the customer,



because frequent attempts to cross-sell can render the customer non-responsive or even motivated to switch to a competitor” (Kamakura et al., 2003, p. 46).

- Additionally, tailoring the bank’s offers isn’t so much about which products and services, rather it is about how these offers are made (as above) and the timing of these offers. This is because there are only a very limited number of bank products and services that are standard and these are also very similar across all the banks.

Interviewee 5 explained this saying:

*There’s not a lot of flexibility around; there is a suite of products, I guess, available but we don’t have flexibility at this level to make stuff up. So, we’ve got to pick something off the shelf that already exists out of the range that’s available. 29/5*

- Cross-selling isn’t limited to the bank’s products and services; rather it extends to those products and services of businesses affiliated/associated with the bank. This might be more prevalent when dealing with SME owner/managers whose lack of time is a factor in accepting advice from a business manager. An example of this was narrated by interviewee 9:

*[Bank name] Securities, which is our share portfolio management product. It might be something they’re into so we can provide that service. You’re bringing in different parts of the bank to what their requirements are. 18/9*

- Cross-selling as strategy was reported to be particularly beneficial to banks in bigger markets such as Auckland where banks face more competition and where seeking new clients was reported to be more prevalent. This was mentioned by a lot of interviewees, two of whom are quoted below:

*Oh absolutely, we would love to do that and Auckland's a bit of a different market where it's actually quite one of the harder markets because people have got stuff – they don't like their risk all in one bank. They'll spread their risk whether it's personal or business through other banks, but yeah that is definitely – we would like everything to be under the same thing, under the same pack. 17/1*

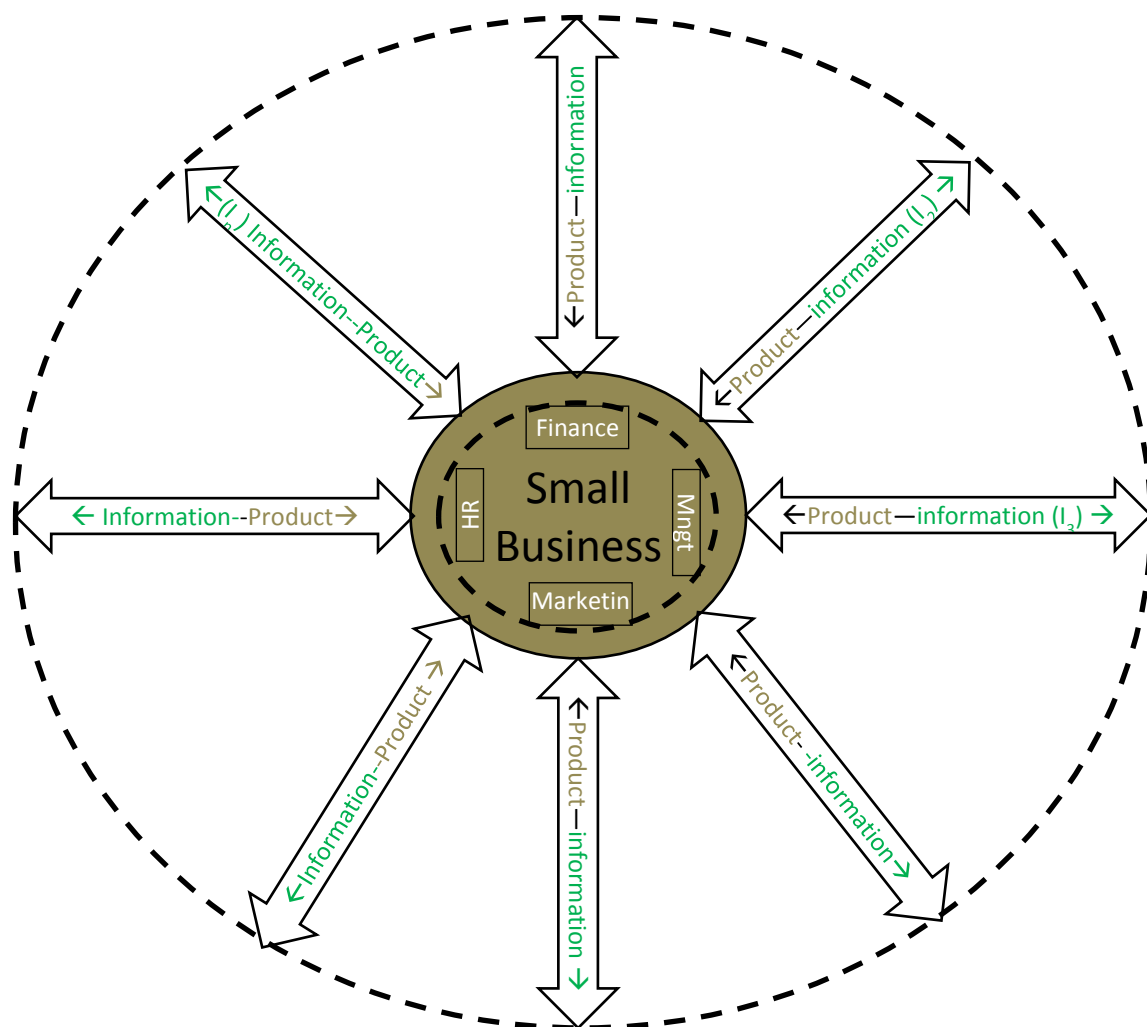
*You don't tread on the toes of a long run relationship there [Auckland]. 3/16*

#### **VI.1.1 Enhancement of assessment accuracy with every product sold**

A trickle down benefit from cross-selling is the bank's ability to enhance its assessment accuracy of the small business client. With every bank product sought by the client (and/or offered by the bank), extra information is required by the bank to process the request. This iterative process of more and different information gathered each time a further bank product is sold, increases the bank's understanding of all areas of interest to its SME clients, hence better assessment can be achieved. This is depicted in Figure 21, below, and further reflected by interviewee 5 who said:

*You understand all the areas of the businesses. I mean, the relationship helps you learn about the business but helps you identify what financial products we can help them with. So, it's kind of a cycle, isn't it? The more you get to know the more you can help, the more you help the more you get to know. 28-9/5*

Figure 21: Cross-selling and the enhancement of assessment accuracy



Finally, it is through this cross-selling strategy that banks aspire to become a one-stop shop for all of their clients' financial needs, with an ultimate objective to increase the bank's revenue by widening a small business's reliance on its bank, and an intermediate goal to

decrease the risk/likelihood of the client changing banks. This customer retention will be discussed in the next section.

## VI.2 Retention

Retention of SME clients was also reported to be a clear benefit of relationship banking. It is achieved in a number of ways. One of these is the *creative entanglement* of the small business clients by way of cross-selling, and consequently these clients find it both hard and expensive to switch banks. The following quotes are reflective of all the interviews on this point.

*It helps the bank in terms of you are a one-stop-shop for all their financial needs so that they get a bigger bite of the spending on that product. And it entrenches the relationship so that other people haven't got that name on their data base and they're not competing with you all the time in order to do things. Not proactively contacting your customers. 28/5*

*You also know that on the other side, the more entangled they are with the bank, the harder it is to leave. So, we call that creative entanglement. I'd rather meet all their needs rather than having some other party doing it. Like we can do their insurance. We can do their debtor finance. We can do their credit cards. We can just; you take the risk away of them going somewhere else because they're not dealing with another bank, and that's what I like to do. So, I like to have everything; you know, credit cards, eftpos, everything here. 24/13*

SME owner/managers find it hard to change banks because of the investment required, particularly in terms of time<sup>31</sup> (Boulanouar & Locke, 2009) and inconvenience (Colgate & Norris, 2001) it would

---

<sup>31</sup> Including time spent away from the main job.

take to switch banks. Additionally, there is the wide spread perception that all banks are the same and that it is difficult to compare banks' costs (Boulanouar & Locke, 2009), hence SME owners/managers see little advantage to be gained in switching banks (Fisher, 2001).

Another way relationship banking is beneficial in retaining clients is through the process of direct and regular contact maintained by the business manager (and/or his account manager) and the SME owner/manager. This was emphasised as being particularly beneficial to banks in guarding their clients from being poached by competitors, as clearly explained by interviewee 3:

*There is a saying, if you don't touch your customers somewhere in ninety days or talk to them, they may be talking to someone else. 17/3*

Several further remarks relevant to this benefit emerged from conducting the interviews:

- Retention includes retaining relationship-managed clients all the way through from small business, to medium, to corporate (please see section V.3 above on taxonomy of the business banking relationship management model).
- As banks retain clients primarily through relationship banking, this could explain why banks advertising on television do not target

their existing clients but rather target new clients through inciting them to switch banks.

- The retention benefit of relationship banking is negatively affected by the number of clients that the business manager manages under his portfolio. This number was reported by all business managers interviewed to be increasing beyond the optimum level that the business manager can deal with effectively. Interviewee 3 expressed this saying:

*That's what worries me a wee bit because there's more customers I get the more I'm just worried that I can't provide the things to; because I used to be able to. When I first started about five years ago I was out visiting customers and I'd visit and I had them on a, you know, six months should be a good thing. Because I'm getting busier and adding more and more, I don't have that contact. 17/3*

Banks are naturally very interested in retaining their existing small business clients, particularly those who are most profitable. Interviewees were aware that attracting a new client was more expensive than retaining an existing client (Kamakura et al., 2003). In fact, it has been estimated that it costs five times more to create a new client than to retain an existing client (Reichheld, 1996). This makes the retention advantage of relationship banking a cost saving benefit, which helps banks to save costs spent on searching for and processing new clients (Gan et al., 2006; Kamakura et al., 2003). Interviewee 15 reinforced this:

*It's expensive to bring in new customers – it's hard to find new customers, and by getting one customer to stay with you for a long time, financially, you're cutting out the cost of doing new things for them. 19/15*

Despite its obvious importance to banks, as demonstrated by its *explicit* mention in all interviewees unprompted by the interviewer, this benefit, retention, doesn't seem to be mentioned anywhere in the academic banking literature.

### **VI.3 Referrals:**

Relationship banking gives rise to new business opportunities or referrals. Referrals involve current clients directly recommending their business managers to other SME clients thereby facilitating the process of gaining new customers. These new clients can be the SME owner/managers' suppliers, their customers, their peers or relatives.

Interviewees 1 and 9 put it like this:

*I suppose from my perspective there's a lot of opportunity to, you know, maybe talk to some of their customers. You know, who they may want to refer or meet to have a chat with.19/1*

*A good relationship means that they [clients] are more likely to refer other people. That's quite common, you'll get other industries, other people in the same industry sort of coming along saying "I've talked to this client and he recommended you and now we want to bring our banking across" so that's common. 12/9*

These referrals cost banks very little or nothing at all. This cost advantage, especially when compared to how much it costs the bank

to gain new clients via other methods (Reichheld, 1996), such as direct marketing campaigns (Kamakura et al., 2003), is significant. A further consideration is that satisfied businesses tend to refer more often, as the banks own research has demonstrated, and as reinforced by interviewee 8 who said:

*Because we know that happy customers will refer business. We know that from the stats. 18/8*

Within business banking, interviewees reported that there are two sources for growing a business manager's own portfolio: their clients, who are considered by far the best source, and accountants, lawyers and other professionals they deal with. Other points of contact like bank call centres and websites were reported to be a very poor source of new clients. Interviewee 14 stated:

*I mean in terms of a marketing tool, most of my new customers that I get come through refers, usually from my existing customers. So existing customers are your best source of referrals – it's always a well-known sort of thing within banking. So building a relationship with your customers is key to you actually being any good at your job in terms of growing your portfolio. So it would be fair to say we'd get very few new customers ring up by going through our internet or through the call centre. We don't get that very often. Usually it's a referral from either a professional or an existing customer, so that relationship side is very crucial. 20/14*

As an example of how a strong relationship with a client can be a continuous source of referrals, interviewee 12 said:



*For example I've got relationships with clients in my portfolio that I'm not their main banker. For example I've got a very good relationship with a customer; we've just done some personal lending for him; he's a business client but he's an influencer within the business community and he can drive other business for me, so just with his suppliers and things like that. So I have a strong relationship with him and looking after his commercial property portfolio, so I look after that plus his personal side of it, but his actual business bank is with [bank name]. 15/12*

Therefore referrals are not only limited to the business manager, but to other bank divisions and units, such as referring a friend or a relative to the branch, rural banking division, or even to the closely associated institutions such as finance companies.

Finally, referrals as a clear advantage of relationship banking were found to be much more prevalent within the different migrant communities such as those from China and India. Interviewee 5 specified:

*The new migrants do value someone taking the time to explain and talk through things and understand where they're coming from and so you do get referrals particularly from the new migrants because they seem to work together as a community so that if someone else comes over and needs a business manager they go, "I've got a business manager, come talk to mine". 31/5*

## VI.4 As a strategy to assess a new industry and gain access to and a foothold in a niche market judged to be lucrative:

Bank-small business relationships have been found to be very useful as a strategy for banks to assess a new area of business<sup>32</sup> and/or a new type of business client, such as new migrants, before a strategic decision is made about the involvement of the bank and to what extent it will be involved.

*New types of businesses in new industries* can be termed as a supply-side driven operation, because it is the bank's wish to understand that market niche/segment. However, in the case of *new types of business clients (SME owner/manager)*, the bank is merely responding to the migrants' specific needs. Thus, this can be termed a demand-side driven operation.

The similarity between the two categories however, is that the bank has to build preliminary relationships with some clients as a first step to understanding that market segment in order to gain a foothold as a second step.

---

<sup>32</sup> To the bank as well as a consequence of new discoveries/inventions such as software firms when they were new.

With regard to how relationship banking is beneficial to the bank when dealing with new migrants, interviewee 5 said:

*Because for me, because I'm a Kiwi getting to know the people that are from different backgrounds it does help because of the way you deliver things and explain things because our systems are quite different and so understanding what their expectations around banking and taxes and things can be quite different and so that relationship gives you the opportunity to understand where they're coming from and what they expect things to be done like and actually the way things are done here. So, yeah, there's quite a steep learning curve depending on where they're from around how the world works here. 31/5*

Banks have taken this to the next step by establishing specific business banking centres in some locations around the country catering for specific migrant groups such as Chinese and Indians and staffed with matching migrant business managers (Guo, Cockburn-Wooten, & Simpson, 2008). Although this is not a completely new phenomenon, the scale of the practice that led to the establishment of migrant business banking units, is new, as explained by interviewee 15 saying:

*Well the bank set up a migrant division in Auckland, to very much get in with those clients. I know – I worked in Wellington in the late eighties and we had a number of – we still had a number of Greek immigrants from the fifties that were in Wellington and we needed to have somebody Greek speaking, and that's why most of the Greek people banked with our particular branch because we would always have somebody Greek speaking available for them. So from that respect, that relationship with the bank is important for migrants as anything else and the easier you make it for them. My father-in-law is Chinese and you can see sometimes when he's speaking English*

*that he's having to sort of meekly translate from his original language into English. 23/15*

Finally, in an excellent example of how a bank used relationship banking to learn about an industry sector new to the banks, interviewee 8 said:

*Over the years we've had various industries come and go so we've tended to hear about them and do a bit of research on them and decide whether it's appropriate, whether you want to be there in the first place. Deer Velvet was a processing industry in this city twenty years ago and not this bank but another bank; we made a decision that that's where we should be involved in and we targeted some key players; just went about it in a constructive basis; got involved with those key players and made sure we understood the industry.47/8*

## **VI.5 Building trust, rapport, and the information transfer process**

It was consistently reported that trust developing out of a relationship banking format is an advantage because the SME owner/manager is encouraged to share information more freely given that they feel secure and comfortable (rapport is established), in addition to knowing and understanding the purpose for which the information is being provided. This was explained by interviewee 7:

*When you have a good relationship the level of communication with your customers is very strong and the trust and the confidence is very strong so there is obviously the desire for customers to be quite comfortable in providing information and also they will understand what information will be provided for. 14/7*

Trust was also viewed as a benefit because it encouraged the SME owner/manager to be open with the bank manager, sharing all kinds of information, both good and bad, as succinctly explained by interviewee 9:

*When you get to know a client, the client opens up and they form a certain amount of trust and they are more likely to tell you the good and the bad. 12/9*

The problems of asymmetric information, adverse selection and moral hazard (Boot & Thakor, 1994; Thakor, 1995) are mitigated by the relationship. Before the loan is approved, the SME owner/manager as the ‘agent’ likely knows more about the project for which funding is sought than the bank manager acting as ‘principal’ on behalf of the bank. As one of the greatest intangible benefits, the benefit of trust means that the SME owner/manager is more likely to disclose more, if not all, the critical information related to the project - particularly that which the bank and/or the bank manager is totally unaware of - yet this information is *proactively* provided. Interviewee 5 elaborated on this point saying:

*I guess it goes back to the trust thing, doesn't it? Then that information if you want it they trust you to give you that information when it's offered proactively by the customer, really, so that things you mightn't even know that are going on they'll explain to you so that you can factor it into which helps the bank in terms of knowing who we're dealing with and what the risk is. 29/5*

A good rapport facilitates the proactive information supply and reflects the level of trust, as interviewee 22 explained:

*All banks have got the same thing; they're all selling the same product, they're all relationship managing their clients in some form. I guess the relationships you've got with the clients are only as good as each individual manager's got with their own clients. And, I suppose the ability to assess it, depending on how much information's coming back the other way, if you haven't got a relationship you're probably gonna be really hard to get that information out. It's either not forthcoming, or you can quite tell that they don't want to tell you, as opposed to, "Look, I know you're gonna ask for all this, and here it is", and happy, or "do you want to ring some of my clients?" Like a guy this morning said to me, "If you want to ring some of these clients that I've got that are doing this, let me know and I'll arrange it." 35/22*

Emerging from the initial interviews, the concept of trust as a key benefit and its relationship to other issues, including the measurement of relationship strength, became apparent and this was actively pursued throughout the remaining interview schedule.

Bank managers develop and use their own yardsticks to measure the strength of relationship banking. The primary type of data they use is soft data. One of the elements they use to measure the strength of the relationship is the level of trust enjoyed with the SME owner/manager.

*There's no hard and fast rule. There's some customers who naturally you just need to deal more often with because of the nature of their business. Being able to have a good joke with a customer is definitely a good pre-cursor to building up a good*

*relationship with them, and I think trust is probably one of the biggest ones as well.*

***Trust will be like for example, I'm one of your customers and I came to see you and say, well I see some trouble in the horizon probably – would that be a good measure then?***

*Yep. Definitely – someone who's quite upfront. If there's any issues – if you get the comfort that they will come to you if there's any problems then that goes a long way. If there's certain customers who you think that if they got into trouble they would do their best not to tell you then that's yeah, also a concern. 36-7/14*

Several business managers reported this to be a more accurate measure than length of relationship, as one interviewee said:

*He may move but he can't find another bank to accept him.*

Traditionally, the strength of relationship banking has been measured by the number of years or the length of the business-bank relationship (Berger & Udell, 1995; Boot, 2000; Duarte & Gama, 2011; Petersen & Rajan, 1994), and/or the depth of relationship banking or the number of products and services sold to each SME client (Duarte & Gama, 2011). The common factor amongst these methods of measurement is that the data collected are hard data, and the collection is managed centrally. Banks, then, have macro criterion which they apply across all businesses. Business managers, however, working individually at a micro level, develop and use their own yardsticks - including trust - with their SME clients. This is a further example of how relationship banking, in the case of SMEs, operates between

relationship managers and SME owner/managers, i.e. person to person, and as explicitly addressed in the literature, between SMEs and banks, i.e. organisation to organisation.

The importance of trust as a benefit of relationship banking was reinforced by all interviewees, who addressed it both from a position where it was present and one where it was absent. Interviewee 21 addressed this second case neatly:

*If the customer doesn't trust us, they won't be forthcoming with information. It's as simple as that. So, if you come to me and you don't trust me, you might say, "Okay. I want to borrow \$10,000 to clear some creditors that I owe money pending receipt of debtor's payments." And that's cool, and I say, "Okay, I'll help you out there." The truth of the matter is you actually owe \$50,000. You don't trust me enough to tell me that. so, rather than address the problem, you just put an immediate band aid on by getting \$10,000 and the real strain on your business is still there. So, if there's no trust in the relationship; if you don't feel comfortable with your banker or vice-versa, the banker doesn't feel comfortable that you're being sincere and honest, you won't be able to make the most out of that relationship. 12/21*

Trickle down benefits from the trust advantage of relationship banking that emerged from the interviews were numerous. One of these resulting from the trust and rapport built up is that of making the bank manager's job easier, as outlined by interviewee 16:

*It makes your job easier if you've got people that you know and you can trust, and they know what you need. So when you're dealing with them you've got no resistance to when you're asking for, for information or even, they know what you're going to want before you are even asked about it, or I know that*



*they're going to come to me and talk to me about it in two years' time ideally. 17/16*

## **VI.6 To humanise the bank**

The humanising of the bank is one of those benefits that was explicitly introduced by the researcher, and no interviewee spoke of it unprompted. However, once introduced all interviewees agreed with the concept and several elaborated on how it works.

While “*Banking is all about confidentiality and trusting*”, as reported by interviewee 8, banks seem to be the least trusted among all business organisations. This is even truer during the times of financial crisis (Edelman Trust Barometer, 2012; Ernst & Young, 2011) where banks are reported to be primarily culpable. All bank interviewees agreed that their SME clients were no exception. Interviewees 8 and 23 elaborated as follows:

*Banks are portrayed as big unfriendly places. 30/8*

*[For] Some people it's a bit scary dealing with the bank because they're going into the unknown. They don't really know bank policies and what they require and that type of thing. 17/23*

The relationship is used as a medium to create an atmosphere where clients don't feel they're dealing with a bank, i.e. a big and innate organisation, especially when banks are viewed as a “necessary evil”. This is achieved by having the business manager as a point of contact who was likened to a “shock absorber” by interviewee 15:

*With customers, I say, “well I hate the dentist, you hate the bank.” But if you think of the dentist, you think of the person who does your teeth, and he happens to be the person that does your teeth. So you’re the face of the bank for that person, and ideally, when they think of the bank they’ll think of you rather than they think of the building or the symbol of the bank or whatever. So, ideally I’ll be like a shock absorber, so the bank’s policy on the road. The bank’s policy whether it’s a car or the road, whichever one, and I’ll be the thing in between just easing the bumps. 21/15*

The relationship manager’s role is to rationalise and *soften* bank policies and requirements for their SME clients. Interviewees 23 and 8 remarked:

*But I suppose it’s breaking down some of those barriers to give them a bit of confidence in who they’re dealing with. 17/23*

*I guess banks are trying to lower that; that barrier as much as possible. 31/8*

Relationship banking is the humanising mechanism through which the relationship manager rationalises the bank’s policy/decisions such as to raise interest rate, to revise down the value of collateral used to secure a loan and/or to ask the SME owner/manager to supply some financial statements more frequently (than before the crisis). It is also a humanising mechanism because the relationship manager softens the landing of these new requirements on the banks’ SME clients.

Despite its importance as evidenced by all interviewees, this advantage was nowhere to be found in the extant literature. However, its importance, according to all interviewees, is significant.

## VI.7 Understand SME owner/managers' motivations for being in business and understanding the story behind the numbers.

Another important benefit that emerged from the interviews is that through relationship banking, the business manager is able to assess the motivations of the SME owner/manager when assessing a loan application from their SME client. Interviewees 16 and 4, emphasising the role of relationship banking when deciphering SME owner/manager motivations, said:

*You can get a feel for what a customer does from just looking at their website, those sorts of things. So, you've got to look at those tools but until you sit down in front of them and have a good chat about life, you're not going to be able to understand what their motivations are. 8/16*

*We've got a lot of individuals in New Zealand that went to university and have run up big, ah, loans. We've got vets with loans of eighty thousand dollars, who go into business and we lend 100% of them buying into a veterinary practice, and yet they've got an eighty thousand dollar government loan behind them. So, their debt, their debt to equity ratio is probably, you know, if you put that through a machine it would go [dur, dur, dur] warning and flash lights in Melbourne and probably in the UN. Um – ah, but those people are not low risk. They've dedicated eight years of their life to learn how to be a vet. They're passionate about what they want to be into. They've always wanted to be vets since they were a little boy. Um – their uncle was a vet. Um – they love animals. They love stroking them. They're going to pay me back. So, the relationship and understanding what makes them tick is the big thing. 35/4*

In explaining what motivation is, and the process undertaken to discover it, interviewee 4 went on:

*I need to know what the driver is. Why, why are you in business? What do you want to get out of this? What is your end gain and why? Miss-- Mr Entrepreneur – who are you? Why are you doing this? I, I've got one customer at the moment; he sells – can I tell you what it is without giving him away? He sells edible product. And his reason to be – one of my manager's customers, is to sell the best edible product in the market. What's that got to do with business? That's; that's religion. That's um – that's hobby. I, I want somebody to tell me what the end game is. How much money do they want to make? How, how big they want to grow this and the reason why they want to grow it. They wanna, they want to leave a legacy to their children? You know, do they want to educate their children? Do they want to bring their children up properly? Do they want to own a house freehold in the quickest time? Do they want to retire early? You know, there has to be a reason why they're in business. 62/4*

Ultimately, a significant number of interviewees outlined how understanding the aspirations and motivations of SME owners and managers facilitates a better understanding and judgement of the accuracy of the information supplied by the SME owner/manager.

Interviewee 4 best explains:

*“Once you understand what makes the human being tick, you understand the information that you're being provided with, and you understand their needs and wants. I think so. I, I think then you can, then you can weigh the information that's coming in to you in terms of accuracy. I mean – for example I had a, um, a guy from Hong Kong who bought his business out here. Ah – he, ah, ah, loaded containers throughout the Pacific on a computer. So, on – he had big computer screens in his home that he - he was out here for lifestyle. He wanted to relocate himself to a safe part of the Pacific, and he could operate out of here. Now once I understood what he was trying to do and what he was trying to do with his children and his, ah, his family, um – and why he was operating, I understood what he was actually trying to do. So then when he provided me information from these big companies overseas that I didn't know, I understood*

*ah, the weighting that these would have because the way he operated with me – he introduced me to the people that he was introduced, and he had the same relationship with them that he had with me, and it gave me, it gave me um – it gave me some more certainty about that relationship.” 31/4*

Motivations behind starting and operating one's own business have been widely studied. These studies range in focus from financial success to expressions of autonomy and independence right through to lifestyle (Birley & Westhead, 1994; Burke, FitzRoy, & Nolan, 2002; Cromie, 1987; Hamilton, 1987; Mason & Pinch, 1991; Singh & DeNoble, 2003). These motivations are considered subjective and personally defined by the individual SME owner/managers and can change as businesses mature. For example, as in the case of SME owners who are not motivated to create jobs for people outside themselves and their immediate families at the start of their ventures (Gray, 1994; Smallbone & Wyer, 2000), however, “it is quite possible that some SME owners do change their attitudes to employment as the business matures” (Walker & Brown, 2004). These issues, besides the intermingling of the personal with the business and the family, make the topic of SME owner/manager motivations very complex (Culkin & Smith, 2000; LeCornu, McMahon, Forsaith, & Stanger, 1996). Relationship banking has been shown to provide bank (managers) with mechanisms to decipher and assess those motivations.

Similarly, the relationship with the SME owner/manager allows the business manager to enquire directly and also to gain an understanding of what lies behind the different numbers provided in the different financial statements. Often, these financial statements are prepared by the accountant or the book keeper but it is through their interpretation by the SME owner/manager that the banking business manager assesses and gauges the owner/manager's financial understanding, financial management capabilities and all the other skills necessary for running his business successfully and their ability to service and pay back the loan. Elaborating on this issue, interviewee 23 said:

*I've been in regular contact with a customer and you know, for example, they were growing their sales or they'd done something – they'd bought a new machine or something like that. Unless you're in regular contact you may not know about those things and if they haven't funded it and that could be a reason why sales have increased. So, I think it does give you a good understanding of the numbers – having a good knowledge of the business which it really is just down to the knowledge of the business and that's only built up through over time and building up that relationship with the customer. But it certainly helps understand financial numbers. I could give you a number of examples of where that would assist. 30/23*

Interviewees provided more detail around the kind of questions that help business managers conduct a comprehensive assessment of the SME owner/manager's financial understanding and financial management abilities. Interviewees 15 and 4 responded:

*[With] an existing customer – and we hear it sometimes; “You can look at our bank account and see what we do.” Yes, we can*

*look at the bank account but it doesn't tell us everything, it doesn't tell us, that might show us some of the cash flow but it doesn't tell us all of the cash flow, and it doesn't tell us where the profit [is coming from] ... 9/15*

*People come along and they're told they need to get a cash flow forecast to borrow from the bank. So come along with a cash flow forecast that has a whole lot of numbers on it. It means nothing. Because where do the numbers come from? I'd rather somebody came in and round thousands did me a rough graph and said, "I need twenty thousand. My income is going to go do-do-do and the numbers go 1-2-1-5-7-3-2 and it comes down; it flows down to some numbers at the bottom," and I look at that and I go, "Yeah, you've done some thinking," and I turn it over – where did that number come from? Why did you have the sales going that way? Where?; Who are you going to sell this to? [Tapping] Who are you going to sell the widget to? How many of these are you going to sell? How big is the market? It's the commentary that counts. Written commentary can be downloaded from the internet can't it, on mass? So, "I want you to tell me what this says" [Tapping]. 61/4*

## **VI.8 Enhanced understanding and evaluation of the overall context around the SME & its owner manager:**

Distilled from the interviews was the idea that understanding the overall context, the engine behind the decision making and rationale behind decisions, interpreting decisions within that context and placing information provided within that context to check its accuracy against the overall plan, is essential, as interviewee 12 states:

*Because theoretically we only see the cash that flows through the bank accounts. So it only gives us one picture. The balance sheet gives us another picture, and actually how they run their business gives us another picture as well. So really if you don't*

*see all basically three of them; you can't do one in isolation.*  
33/12

The relationship model allows this to happen and also provides the overall context in which it can happen.

As detailed in Section V.4 above), the process of loan underwriting for relationship-managed SME clients involves the assessment of three main things: financials, security and character. The financial statements are but one valuable source of information to assess the credit eligibility of SME borrowers. Equally important are the other sources of information such as collateral pledged by the SME client and market conditions supplied by the bank's economics department. What the relationship banking model allows the bank (manager) to do is to combine all those sources together enabling the business manager to complete the picture/jigsaw about the SME and make a final decision.

This provision of a comprehensive context of the SME owner/manager's business environment is consistent with the relationship banking definition developed in this study (please see section V.5 above).



## VI.9 Access to and assessment of Intangibles:

*It's very hard to capture things that fit outside the box in a system, and I guess the business banking<sup>33</sup> tends more for things to sit outside a box rather than within it. 19/19*

The relationship is used as a way to deal with non-standard issues/things that were reported as the hallmark of business banking.

The relationship model is unlike rigid models, such as credit scoring, where pre-existing boxes are filled-in for an application to be processed and if anything falls outside of that it just doesn't get processed. With the relationship model, one of the aims is to try to identify, capture and work on/process things that fall outside the box, as neatly summarised by business manager 19 (above).

Interviewee 3, who used to be a branch manager, explained this further by way of this example.

*But my philosophy with my staff was, if you can't help someone with a mortgage then go to one of us and talk it through and see if we can do it another way. And I've helped people to do it another way because it's not always, you know, blinkers on. So, you've gotta look outside the square and then once you've looked outside the square and you've done all you can then you can go say no. 10/3*

Issues that are outside the standard parameters include not only *content* issues but also *form* matters, where the usefulness of relationship is clear, as explained by interviewee 21.

---

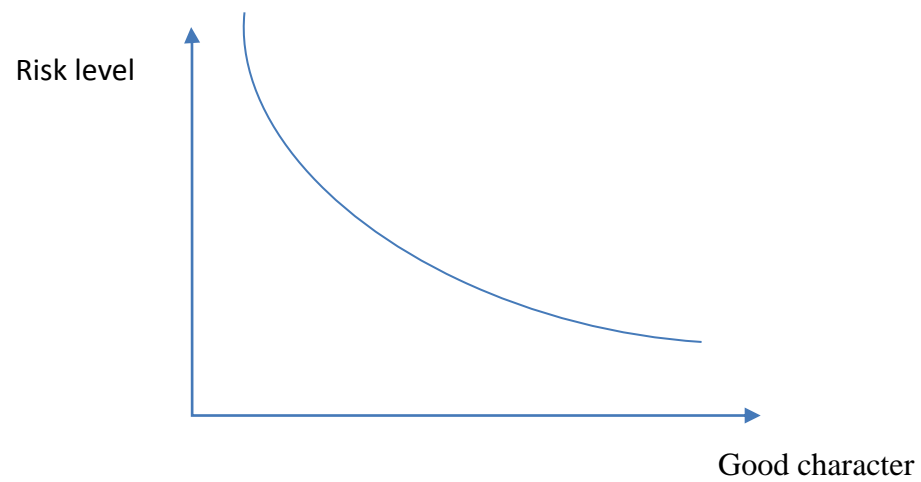
<sup>33</sup> Referring to relationship banking

*Look, there's a lot of interview models or processes that you can go through, but it's really about establishing rapport, asking permission to profile, understanding what the customer wants; you know, summarising your understanding of their needs. If they have any objections, handle those objections with respect; get buying for the proposition or the scenario that you suggest to meet their needs and then establish the next steps and who's responsible for; ... But you can't get too prescriptive. Yeah, with the model, because you have... in a true relationship you have to show a wee bit of intelligence. You have to at times be empathetic. Sometimes you've got to be sympathetic. Sometimes you have to be firm. You know, so I don't think any one model fits all. A model is okay for guidance but you know, in this day and age, you've got to show a wee bit of maturity and flexibility to meet the customers' needs. 12/21*

A related discussion is that of intangibles. Intangibles are defined as assets with no physical properties (Corman, Pennel, & Lussier, 2008) such as a patent, good reputation or, as discussed here, the SME owner/manager's business acumen. Without relationship banking, banks assess the intangible assets by using evaluating proxies which are indirect methods of evaluation, such as using number of years spent on the business by the SME owner/manager as a proxy for his business capability to operate his small business successfully (Duarte & Gama, 2011). While these indirect methods are useful, the use of relationship banking allows banks, through their business managers, to directly evaluate intangible assets, such as character, by assessing the SME owner/manager's two key qualities - integrity and capability. Furthermore, from the interviews, owners with good character, i.e. high integrity and good business ability, are apparently more successful at overcoming obstacles and meeting their obligations

regardless of the conditions. In terms of risk management, this points to an association between good character and lower risks, and means good character is synonymous with a lower risk to banks as per Figure 22, below.

Figure 22: Risk level as a decreasing function of character reputation



Relationship banking is therefore a mechanism with which to gain access to and assess the intangible assets, as explained by interviewee 3 when talking about the character:

*That relationship is getting to know the customer and getting a feel<sup>34</sup> for what they're like, and that's just by asking questions you know, understanding what their background is, where they're from, what they want to do. And I'm thinking of new customers there. My other one, we go out and visit our customers, and from that we find out things. It may be an anniversary or things or that they need things done or things have changed in the business or they need a bigger overdraft or they need a loan. 13/3*

---

<sup>34</sup> i.e. to understand and assess

Interviewee 8 cemented this benefit of assessment through visiting work premises, saying:

*Yes, we would use that [relationship] as an assessment tool as well. ...If I went out to his factory and found that he was paying them less than the minimum wage; that would concern me. If I found that he was cutting corners and breaking laws that would certainly cause me trouble. 40/8*

Not everything can be assessed through the hard data provided by the SME owner/manager and/or their accountant. Similarly, “not everything can be credit checked” (interviewee 4). Explaining the process of how access to and assessment of soft data is done, interviewees 4 and 12, respectively said:

*The only way you can find out most of this information is to actually talk to somebody. It's not public knowledge. So it's not in the public domain. So, yeah, that's probably another reason why we need; you know, we're dealing, we're dealing with the inner most lives of people. You know, we know a lot of stuff. We know a lot – potentially we know a lot, a lot about people that is not in the public domain. Um – and there's stuff that we need to know about a person that's not in the public domain. You can't credit check for everything. That is a huge benefit to the bank and for the customer I think it's a benefit as well. A lot of customers will share stuff with their bank manager that they won't share with anybody else. 55/4*

*Look at them in their own environment, see what their business does. 34/12*

By way of two concrete examples, interviewee 12 illustrated the way the relevant intangible data is accessed, processed in context, and transformed into information that can be evaluated within the wider context.

*I take my food distributor. He starts work at four o'clock every morning. No balance sheet or anything is ever going to tell me that. He finishes at four o'clock each day, so he works a twelve hour day, but you don't see that. You don't see; does he actually work in the business? Does he drive the truck? Does he not drive the truck? How does he interact with the staff? Do they respect him? You don't get that off a balance sheet. You're not getting that off financial information. You look at a truck. You go and see a truck. You see how well it's maintained. Is there oil leaking all over it? Is it filthy? So do they do their maintenance on their trucks? Do they not do their maintenance on their trucks? How often? That's a visual thing, and that's part of relationships because I can't really help a customer if I don't really understand what their business is, and so as I said, but as I said, I don't need to know exactly in and out how to make a circuit box or a TV company or someone like that. I don't need to know that but I need to know, well this is what they actually do because take one customer that I've got is an electrical contractor. Ok now they do 60% work on farms. They do 40% for the local council. Farming – the bulk of its dairy farming but if I didn't know that; if I just looked at a balance sheet and looked at the figures and didn't know the breakdown of those sales then I wouldn't be taking any interest in what's happening in the farming community at the moment, so the price of milk's gone down; okay what they're getting paid so that has influence on are they going to be doing maintenance? Are they not going to be doing maintenance, so when I see him I ask him how that industry is, so we're looking at concentration risk? So are they in with one supplier? Who's their suppliers? Do they then have an exchange rate risk? So you don't see that type of thing from a balance sheet. 34-5/12*

## **VI.10 To understand, assess, and mitigate risk around/related to the SME owner/manager:**

'Character' assessment is a special case of intangible data, and because of its paramount importance (as per section V.4.1.3 above), this section deals with the character of the SME owner/manager in more specific detail. Relationship management was reported to be the

best mechanism to properly identify and understand the risk around the SME owner/manager, assess that risk and finally, try to mitigate it.

Dealing with all these issues respectively, interviewee 4 said:

*Without a relationship, if we were just lending to entities without seeing the human being behind the entity, I think we would have a wrong, the wrong weighting on risk...[because] businesses, businesses don't go broke; people make the wrong decisions. So, knowing the person behind it I think is a correlation to – the more we know the person, and we make the decision on that knowledge, the less likely we would have a loss.” 35/4*

*“You ask the questions about – so going back to the character, um – I think you can ask a series of questions that mitigate some of the risk. I mean if somebody's lying to you um – and, and knows what you want to hear they'd have to be very good at it – they can still get through, no doubt about that. My junior managers could probably be more easily lied to than my senior ones, but all people can be fooled. But I think the more people that you see, the more deals that you see, the more you understand the – entrepreneurs, you understand what drives people. I think you get a feel for it pretty quick, and it's harder, it's harder and harder for you to be fooled.” 21/4*

Furthermore, relationship banking facilitates a better and more complete understanding, and so assessment of risk around the SME owner/manager is by virtue of allowing the business manager to do a more detailed analysis of the SME owner/manager (the 'what') and combine hard and soft data (the 'how'). This use of the relationship banking model is demonstrated by interviewees 6 and 18 respectively.

*[Relationship] helps because it helps to really to back up the loan because you know you can demonstrate that the customer is good at doing a business or is good, isn't good. You can*

*basically go through the strengths and the weaknesses more than if you're just doing an automated type situation. 17/6*

*...Relationship is important because you know what the customer is about; you know who he is and what he's doing. The intangible side of things, yeah you can't assess that without actually having a relationship I don't think. You can look at the assets and the business but who's the person? Can they run the business? It's crucial – they can have all the assets and if they can't run the business, it fails because they're not the right person doing it. So the relationship banking model allows you to actually have a full understanding of that client and be able to make informed decisions I guess.18/18*

Two real examples follow of how business managers managed to identify and assess risks that were destined to go unidentified if it weren't for relationship banking. The value of these examples resides in how the relationship helps the bank in reducing type I errors related to intangible risks.

The two examples were reported by interviewees 4 and 5 respectively.

*I knew that a customer was beating his wife. OK? And I found out this because um, I had a regular lunch time gathering with um, bankers from all the different banks at the [place name] club where I was working in [place name]. Ah – accounts in the area, insurance assessors and agents, lawyers, and there was a bunch of about anywhere between fifteen and thirty of us in the local area and we met once a month for a meal and we talked over a meal and a bottle of wine and we discussed what was going on, and whilst we didn't use too many names, the names that came up are the type of people in your society that are rat bags. Um – this guy had a wonderful, wonderful business. Ah, he was going into expansion mode and he ah, all his assets were joint and he was taking some risks, and he didn't bring his wife with him and I knew he was beating his wife. So, everything stacked up and I said, "No." And I let it go to another provider because I knew that there was more at risk in the deal than the numbers show. So, it's not all about*

*understanding the numbers. You can't mitigate for that risk. You can't add a premium on to that risk without letting the person know why you're adding the premium on. So, there's some stuff that you can find out um, that you know from your general knowledge which is soft data that you can't input anywhere on a, on a sheet so you just don't do the deal and you turn it down flat. 66-4*

*An example of an application that ticked all the boxes and passed and about two days prior to settlement the – maybe not quite but just before settlement, like, from between the application, the settlement date there was a property purchase the people involved sacked their professional trustee. And then they sacked their solicitor. And to me this was saying that they were getting advice that they weren't listening to and their relationships around them were breaking down. And so we didn't proceed with that deal because I lost confidence that the people involved – the people I know in the community – who are top quality professionals and if they're giving advice to their client and their client chooses to sack them rather than listen to the advice it suggests to me that there's stuff going on I don't understand. And so I wasn't comfortable proceeding. 32/5*

Relationship banking also adds value by way of reducing type II errors related to intangible risks. Interviewees were presented with a hypothetical scenario where a loan application was received from a SME owner/manager to buy the competing business next door. The application ticked all the boxes except that, over the years, the relationship manager had noticed a high turnover of the only two employees working for the business. This was interpreted by the business manager as the SME owner/manager having trouble retaining his employees. This didn't seem to impact the running or performance of the business. However, with an expansion plan on the table, this potential employee retention problem was likely to be compounded.



From this scenario, if the bank was reliant on hard information alone, it would likely accept the SME owner/manager's loan application to extend his business, as the financial statements and other documents didn't show anything about the turnover of employees. However, the relationship model not only allowed the bank to identify the risk but also to suggest a way to mitigate that risk, as summarised by interviewee 8 saying:

*Well it's a benefit for us. It may not be a benefit for him but we would certainly take that into consideration – the good, the bad, and the ugly. The good is because of this; there's a lot of good things he does there as well, so that would be on his plus side. We'd be realistic and say, "Look that's a question mark let's see if we can sort of put some sort of framework around that." We would ask him, and if he came, "Look I hear what you're saying but it hasn't been a strength of mine but I am going to employ a human resource manager." That would mitigate that one. 49/8*

It should be noted, however, that the scenario itself was seen to be 'unrealistic' by the majority of interviewees.

## **VI.11 Developing the soft-data benchmark**

### **system:**

A benefit deducted from the interviews, although not specifically identified by interviewees and totally absent from the literature, was the 'soft data benchmarking system' (SDBS).

From dealing with a range of SME clients on a one-to-one basis through relationship banking, the business manager is able to construct a mental map of patterned similarities and differences between these clients (by industry sector, geographical area, age of the business, etc.) leading to him/her having the ability to construct a written or unwritten database. However, unlike a database constructed by the bank using hard data sources such as the clients' cash flows and balance sheets, the database constructed by business managers is soft-data base, hence the term Soft-data Benchmarking System (SDBS). The construction of a Hard-data Benchmarking System (HDBS) and how business managers use it was explained by interviewee 3:

*We have a sort of a check system in the bank; we have a system in place which has got the various industries, and what they've done is analyse their cash flows or their balance sheets and this is a medium business, you know, a small-medium-large and best practice and it shows what profit they should make as a percentage in everything is, what the turnover usually is, what the percentage of expenses are; its gross profit and all this sort of thing. So, when we get a cash flow we can do what is called a reality check. From other people in industry, and of course if it's higher than someone else; it says, "What are you doing different?" Please explain. 4/3*

The SDBS conforms to the definition of knowledge-based system (Akerkar & Sajja, 2009) as an organised body of related information systematically collected and stored by the business manager with instant access, searching and sorting abilities as well as constant updating and analysis. This collection of experience allows the

formulation of benchmarks against which the business manager can compare each new business situation the SME owner/manager faces.

A contrast between the HDBS and the SDBS is summarised in Table 16, below.

**Table 16: A contrast between the HDBS and the SDBS**

	<b>HDBS</b>	<b>SDBS</b>
<b>Data benchmarked</b>	Hard	Soft
<b>Collector and assessor</b>	Mechanised / automated	Business manager in person
<b>Subject</b>	Small business as a firm	Mostly SME owner/manager
<b>Types of institutions</b>	All financial institutions	Relationship-based banks

In the same way they would use the HDBS, as explained by interviewee 3 (above), business managers can use these SDBS in many ways; for example, to detect anomalies in the behaviour of their clients and to seek an explanation as to the source/reason for these anomalies. A second use is to check the credibility of the client, particularly those new clients and/or those clients whom the business manager doesn't know very well (yet). When business managers detect an anomaly they refer to the SDBS, and in most cases, are able to predict the cause of the anomaly at this point and instead of introducing the issue, a business manager would wait for the SME

owner/manager to explain the situation. This allows the business manager to make a comparison and, upon the completion of that process, the business manager would be able to update their assessment of the client's credibility.

Knowledge building practices such as SDBS can be argued to be one of the points of difference between banks that use relationship banking and other financial intermediaries, and non-users of relationship banking. This contributes to answering Puri et al. (2011)'s open questions for future research on whether, and if so how, banks use this information. It is also relevant to questions concerning other types of business and for other customers such as for example corporate customers when these customers apply for a loan. It allows banks to learn about their SME clients, and the market conditions they operate in in real time, because as interviewee 14 said, this is only possible from interacting directly with the clients, giving banks a head start over other financial institutions:

*I mean most of it is got through experience anyway that you can only get sometimes on the cold fact of talking to customers because you don't read about it in the newspapers and things, and so you know we probably knew the recession was hitting two months before anyone else because our customers were starting to find things really tough and the media and the statistics are always quite lagged in terms of what comes out of the market.19/14*

This knowledge building through talking to clients seems to be encouraged by banks, as explained by interviewee 4:

*I think relationship banking is knowing our market, knowing our customers. It's about, it's about knowledge; knowledge is power. I would expect my senior managers to be able to give me a commentary of their market. Um – and give me a commentary of ah, what's actually happening up there, and they would have examples of customer-- what customers have told them. So, I don't want them regurgitating what's in the New Zealand Herald. I want them to have an opinion about how their market is operating here. 35/4*

These individual SDBSs, developed by each and every business manager, must be pulled together at the bank level, and then organised by a specific criteria such as industry sector, geographical areas, economic cycles, or size of the business<sup>35</sup> into a bank-wide SDBS.

Future research could develop a best practice model of how this could be achieved.

## **VI.12 Information reusability:**

A benefit introduced by the interviewer was information reusability which concerns the bank (manager) not having to re-invest resources such as time (and/or money), as a factor of production, to collect a piece of information that is needed (or already gathered); for example, to process a loan application for an existing relationship-managed small business client. It is particularly important in relation to time, as

---

<sup>35</sup> Other classifications could be per education level of the SB owner/manager, his/her ethnic background etc.

time was reported to be the biggest cost, as explained by interviewee 4:

*Time is the biggest cost. Labour, labour is our biggest cost as a bank. 44/4*

Information reusability is beneficial in three ways, as discussed in the literature review (section II.7 above). However, in its third form, reusability across-clients, it is linked to the SBBS raised in the previous section (section VI.11 above). While the business manager might not yet know the new SME owner/manager client, from dealing over time and across a range of products and services with other similar businesses, the business manager is able to *re-use* with the new client the information s/he has previously learnt without having to relearn it. The business manager might even be better placed than the new owner/manager to consider the prospects of the new venture.

Illustrating some of these points, the following quotes from interviewees 21, 2 and 8 respectively were:

*So, you and I meet for the first time and we understand each other; we get a good vibe about each other. We don't have to go through that same rapport building again. So, we just hit our straps, 'Great to see you again John. How can I help you today?'. 22/21<sup>36</sup>*

*I wouldn't ask. Two years down the track hopefully I don't have to ask are you married?; how many kids you have? - so things like this.30/2*

---

<sup>36</sup> Particularly soft data which is not standardised to be filed in a file and is kept in the banker's head.

*It could be electronically retained and I could easily whip back into that and locate it...All that information would be on our file already and some of it will be processed so it's a matter of just revisiting that.45/8*

As confirmed by interviewees, information reusability is particularly beneficial for information that does not need any updating, such as the location of the small business premises. Even with information that has to be updated, the bank manager need not get involved as the account manager usually takes charge of such tasks, thus freeing the bank manager to do more lucrative/important things from the bank's perspective as can be understood from interviewee 9 saying:

*The way that it works within [X] bank is that under this business banking where you've got borrowing under a million dollars; my job as a business manager is actually to go out and meet people, get the funding approved, whether it's under my own discretion or whether it's I've got to put an application to the bank and get it approved. By bringing the client on board get everything up and running, bank accounts, the whole thing, all set and ready to go and then what I do is I pass the day-to-day management and the relationship onto an account manager. Okay, because under this scenario here it would be nothing to bring on five new clients a week. That's something I can do because I'm not involved in the day-to-day management and relationship with the client.10/9*

Information reusability is a benefit that can be claimed from using different lending technology, such as that of an asset based lending technology. However, for the purposes of this study, it is important to point out that it is also a benefit of relationship banking. Further, the relationship banking model allows the extension of this information reusability benefit into soft data, which enhances its depth and value

as information to the business manager (please see Section VI.11 on the SDBS).

### **VI.13    Reduction in the marginal cost of information production and spreading the fixed costs of products:**

As with other benefits introduced to the interviewees, such as humanising the bank, reduction in the marginal cost of information production and spreading the fixed costs of products were benefits that had to be introduced. However, unlike the humanising benefit, where the mere introduction of the benefit acted as a trigger generator idea, these benefits had to be explicitly followed up; and even then, some business managers did not recognise these as activities undertaken by the banks, or benefits for the banks, as interviewee 13 said with regard to spreading the fixed costs of production.

*I don't see how we can do that because a lot of our things like credit cards and insurance are all quite vanilla and the pricing is advertised or whatever; it's quite clear. No, I don't know that we'd do that. 29/13*

Contrary to senior managers who would view both the reduction in the marginal cost of production and the spread of the fixed costs of products as important benefits, most of the business manager interviewees considered them insignificant. This is because business managers are not fully aware of the product pricing schedules and



their allocations as these are decisions taken either at head office and/or at a higher managerial level.

This lack of awareness of pricing of bundles of bank products to SME clients by business managers is illustrated by the focus (fee establishment charges and insurance) of the responses from interviewees 23, and 11.

*If you've maybe done a major transaction and there was some costs and like a fee establishment charge and then they were looking to add an additional service which had a cost to it as well maybe in close proximity to that transaction, we might consider that the cost would be reduced due to having just paid the establishment cost. 29/23*

*The instance is if you've got car insurance you don't get any discount but if you've got house contents and car insurance, you do get a discount. 23/11*

It is well established in the literature that the spread of fixed costs is an important strategic benefit to banks. Bakos and Brynjolfsson (1999) showed how “a strategy of selling a bundle of many distinct information goods<sup>37</sup> for a single price often yields higher profits and greater efficiency than selling the same goods separately” (p. 1627).

Business managers, then, need to be fully trained on the existence and structure of all benefits, so that the benefits can be maximised for the bank.

---

<sup>37</sup> Defined as goods with zero or very low marginal costs of production (Bakos & Brynjolfsson, 1999), which is the case here.

## Conclusion

This chapter has reported on the thesis's findings, analysis and discussions on benefits accruing to banks from the use of relationship banking with their SME clients. While there are several ways to classify these benefits as will be shown below, two classifications are discussed in this conclusion, and a rationale provided for the value of these classifications to banks. Following this, the fully developed Matrix 1 below, listing all of the benefits that were discussed in this chapter and specifying/classifying each benefit within the taxonomies developed by this thesis, is presented.

As noted in the literature review (please see section II.7, page 64), there is no single work that has been entirely devoted to the topic of the “benefits of the bank-small business relationship to banks”, but on the basis of scattered ideas in different references, it was possible to prepare a list of benefits. These benefits are labelled *literature-benefits* due to the source from which they were derived. The second type of benefits were those that were inspired by the literature review, but did not come straight from it and were from the author's “thought experiments” (Lave & March, 1975; Maxwell, 2005). These benefits are labelled the *theorising-benefits*. The third type of benefits are named *emergent benefits*, as those were the benefits that interviewees

were the first to talk about and explain but that the banking literature was/is silent about. The fourth and last benefits, termed *new-benefits*, are those that this research claims to have discovered in their articulation and conceptualisation. These benefits are derived from analysing the data. The findings around these new benefits have important implications for the current research in regard to comparative studies of the different lending technologies in general and, more specifically, to the future of relationship banking which is challenged by an increasingly competitive financial markets such as the use of online banking (Han & Greene, 2007).

In terms of classification, considering the different steps that a loan application from potential small business borrowers goes through, from the preparation before the application is lodged with the bank right through until after the loan is paid back in the case of a successful loan application (or declined in the alternative case), the relationship banking benefits to banks can be traced along this time line. This means that the benefits can be classified into at least three distinct intervallic periods each marked by the endpoints ‘before the application’, ‘during the processing of the application’ and ‘after the application’. The value of this classification resides in a number of strategic decisions made by the bank. One such strategic decision is the training of the person in charge of processing the loan application

during the interval of time marked by the endpoints mentioned above, hence maximising the likelihood of securing the benefits occurring during that period by providing (for example) a list of benefits that that person is to look for and/or training him/her in how to secure and maximise those benefits.

Considering a conceptual definition of the discipline of finance as lowering risk and/or increasing return (Gehr, 1979), and from the detailed study of the benefits reported in this chapter (V), the relationship banking model can be conceptualised both as an assessment mechanism - to assess and lower risk - and as a marketing mechanism - to increase return. Since banks are in the business of increasing wealth of their shareholders (Koch & MacDonald, 2009) by way of increasing return and managing risk, the second classification of benefits could be termed the assessment-marketing (or risk-return) classification. This is because most of the benefits that this study has established can be allocated under those two categories: *assessment* and *marketing*; the two arms of a bank's ultimate and overall objective. The *assessment arm*'s role and objective is to lower the bank's risk, such as by assessing the intangible side of the small business owner manager, his business understanding and management ability. The *marketing arm*'s role and objective is to increase the bank's revenue, for example by way of cross-selling, customer

retention, and referrals. The value of this classification lies in its usefulness to, for example, systematically prepare the bank employee by way of training in marketing and/or risk assessment and provide an ideal and achievable support system to ensure maximisation of the marketing and assessment benefits to the bank<sup>38</sup>.

Matrix 1, below, provides a nomenclature of all the bank-SME relationship banking benefits accruing to banks as established by this thesis. Each benefit is specified within the categorisation and the classifications as explained above. Regardless of the type of classification adopted, however, the benefits mentioned by the literature were found to be quite negligible in terms of importance to the bank managers, some interviewees even viewed some of them as ‘There Just to Increase the Number<sup>39</sup>’. Most of the emergent benefits, along with the theorising and the new benefits were found to be substantial. This shows the significance of the contribution made by this research. The next chapter concludes the thesis.

---

<sup>38</sup> Other possible classifications exist such as dividing benefits into root-benefits and trickle down or consequential benefits i.e. those that are corollary benefits of the root-benefits.

<sup>39</sup> Is a Chinese idiom with a negative tone. It’s a metaphor to say an unfit person tries to pretend s/he is capable of something great or inferior goods pretending to be qualified goods.

**Matrix 1: Nomenclature of bank-small business relationship benefits to banks**

Benefit	Type				Classification 1		Classification 2		
	Literature	Theorising	Emergent	New	Assessment	Marketing	Before	During	After
Cross selling:	X					X			X
• Enhancement of assessment accuracy with every product sold (as a corollary benefit)	x				x				x
Retention			X			X			X
Referrals			X			X			X
As a strategy to assess a new industry and gain access to and a foothold in a niche market judged to be lucrative				X	X	X	X		X
Building trust, rapport, and (promotion of) the information transfer process			X	X	X	X			X
To humanise the bank		X		X		X	X		
Understand SME owner/managers' motivations of being in business and understanding the story behind the numbers.			X		X		X		
Enhanced understanding & evaluation of the overall context around the SME & its owner manager				X	X		X		
Access to and assessment of intangibles					X		X		
Developing the soft-data benchmark system				X	X				X
Information reusability	X				X				X
Reduction in the marginal cost of information production	X				X				X
Spreading the fixed costs of products	X				X				X

## **VII. Conclusion**

The findings of this thesis have several implications for policy, practice, and concept and education agendas. As such the format of this chapter will address these parameters as they relate to each of the thesis four research questions.

### **VII.1 What does relationship-banking mean to the five major bank brands in New Zealand?**

Currently no precise definition of relationship banking exists, as it is commonly defined by what it does not what it is. Additionally, the definition that banks and bankers work with is different from the definition in the literature (Berger & Udell, 2006; Boot, 2000). Bankers consider relationship banking as an overall model, not just a lending technology. This lends a crucial element to the definition of relationship banking or, even, redefines it vis-a-vis Berger and Udell (2006). With regard to Boot (2000) definition, an element is missing from the perspective of banks and bankers, and that is the one-to-one management model which is simply not possible when using his definition. The implications this has for the concept are three:

- i) relationship banking is an overall model and not just a lending technology as, for example, credit scoring is;
- ii) The consideration of one-to-one management needs to be explicitly added to the academic definition;
- iii) Relationship banking is, at least in the case of SMEs, not just organisation-to-organisation (bank-SME), but also person-to-person (relationship manager and SME owner/manager).

This explains formally how: first, when either (or both) relationship manager and/or SME owner/manager changes, the relationship banking model changes and second, the issue of delegation of decision making to the relationship manager from the bank side is valid (Berger & Udell, 2002).

Implications for the research agenda point first to the necessity to check the claim made here. This can be done by testing the differences between the one-to-one relationship banking management model and the effects on assessment accuracy and profit level or bank performance, and then making an assessment of certain aspects of the project(s), such as whether SME owner/manager business acumen is critical to the success of the project.



The potential outcome here is an adjustment to the academic definition and, consequently, a significant improvement in the understanding of the phenomenon. This is because it is from the definition that the decision of what to measure and how to measure it is made. So, if we are to properly study relationship banking, we need to measure different aspects of it including one-to-one management and its consequences, compared with the many-to-many.

Further findings concern the taxonomy of relationship banking. This finding consists of the identification of three different levels of relationship, and enables the creation of a taxonomy identifying end points between the three levels. Academics have to be cognisant of the existence of different levels of relationship banking, although to date, the literature does not reflect any such cognisance, and this will naturally impact on the accuracy of outcomes. For example, rather than one single cost-return function, there is a cost-return function consideration for each of the three levels. In practise the implications for bank policy are (i) banks should expect a return function in proportion to the cost function of each level, (ii) an appropriate evaluation of each segment's performance assessment needs to be done based on all the costs and returns to that specific segment, and (iii) it is only through the separate evaluation of each segment that the bank would be able to perform an

appropriate investment decision making in terms of, for example, how much resource allocation is required for an optimised return to each segment.

The main concepts here are the ability to make a better assessment of each segment, to separate out the contribution of each segment from the whole, and to better solve issues that might be specific to each level such as in the case where the bank had moved to a more phone based management model as it was found that managers didn't have enough time to properly serve the clients in their portfolios.

This finding offers several opportunities for future research. The different levels of relationship banking, including cost return functions using, for example, a piecewise type of function could be mathematically modelled and the model generated could be empirically tested. It would then be possible to see if other relationship banking contexts have the same or similar levels. (An obvious first context would be Australia). Further, it could be confirmed that banks do actually address the three points above.

## **VII.2 How does relationship banking actually work?**

In New Zealand, relationship managers use a different variant of the cannons of lending (5C's). Pivotal in the New Zealand context are

financials, security and character. Of these, character assessment is paramount, and the relationship manager makes this assessment. In contrast to this, a key finding is that as online businesses are not directly assessed in their character, that is, they do not have relationship managers assigned to them, a comprehensive assessment of character is missing in their case.

The key concept here is that understanding how relationship banking actually works may help improve online businesses' access to bank borrowings.

### **VII.3 What are the sources of value (i.e. benefits) of relationship banking to the five major bank brands when dealing with SMEs in New Zealand and how do these banks secure these benefits?**

The thesis identified sources of value relating to relationship banking which accrue to banks as 14 benefits. The thesis has been able to answer the decades-old question concerning how those benefits are secured, namely "existing empirical work is virtually silent on identifying the precise sources of value in relationship banking. For example, while it is very plausible that banks acquire valuable information through relationships, and the empirical evidence is generally supportive of this,

little is known about how banks obtain information, what type of information they acquire, and how they use this information” (Boot, 2000).

Further, this study has identified and conceptualised new and valuable benefits (an example is the humanisation of the bank) and has also shown how to secure those benefits. The findings around these new benefits have important implications for the current research in regard to comparative studies of the different lending technologies in general and more specifically to the future of relationship banking which is challenged by an increasingly competitive financial markets such as online banking (Han & Greene, 2007).

The changes to practice indicated by the findings are for banks to develop a list of all relationship banking benefits and make all their relationship managers aware of all of those benefits because relationship managers are not (fully) aware of all the benefits. This thesis also suggests banks use the classifications of relationship banking benefits herein.

The development of a training course for banks’ relationship managers on the sources of relationship banking benefits and how to secure them is also recommended, rather than simply relying on just relationship managers learning about these benefits on the job as is currently the case.

Veteran relationship managers could also be made aware of the new benefits identified by this study and how to secure them.

A key concept here is the improvement of banks' processes for securing all relationship banking benefits.

In terms of future research, a best practice of relationship banking benefits based on the sources of value identified by this study could be developed. Further research could be conducted into other relationship banking benefits and investigating how banks secure them. It also offers the opportunity to quantitatively test the newly identified benefits.

Other equally important contributions of this thesis include the classification of all the benefits identified and categorisation of them into taxonomies, such as increasing return and/or better assessment benefits, leading into defining and positioning relationship banking within/at the heart of finance as both an assessment tool/mechanism and a marketing tool/mechanism to both lower/mitigate risk and increase return as per the definition of the finance discipline.

From a practice perspective, banks can use the classifications identified by this thesis, and potentially other taxonomies, that might be more suitable to the objective(s) at hand. Bank managers can be educated about these classifications helping them identify (what and when) opportunities to add value (and how) through relationship banking. The

classifications can also be used to help bank managers become fully aware of the dual use of relationship banking as an assessment tool/mechanism and as a marketing tool/mechanism.

The key concept underlying this finding is that it can improve banks' performance in terms of risk assessment and increasing return. Finally, a research application of this finding is that empirical studies can be designed to test and measure the key result put forward by this study: relationship banking as an assessment tool and a marketing tool.

### **End note:**

During the course of undertaking this thesis, the following related conference papers, journal article and presentation were completed.

Boulanouar, Zakaria & Locke, Stuart (2009), “Cost of small business banking: A New Zealand study”, *Service Business: An International Journal*, 3 (3): 211-227.

Boulanouar, Z.; Locke, S. and Qi, W. (2007), An analysis of the cost of banking for SMEs, *Small Enterprise Conference 2007*, Manukau City, New Zealand; 23-26 September, 1-13.

Boulanouar, Z. and Locke, S. (2007), “Small businesses in New Zealand and the Cost Consequences of Bank Choice”, *30th Institute for Small Business & Entrepreneurship Conference*, Glasgow, Scotland; 7-9 November.

Boulanouar, Zakaria (Oct, 2010), “A match made in heaven – the bank-small business relationships: what’s in it for banks?” ‘Thesis in 3 Minutes’ finalist (61 entries), *University of Waikato*, Hamilton, New Zealand.

## VIII. References

- Akerkar, R., & Sajja, P. (2009). *Knowledge-Based Systems*. Sudbury, Massachusetts: Jones and Bartlett Publications.
- Alasuutari, P. (1995). *Researching culture: qualitative method and cultural studies*. London: Sage Publications.
- Allen, L., Saunders, A., & Udell, G. F. (1991). The pricing of retail deposits: Concentration and information. *Journal of Financial Intermediation*, 1(4), 335-361.
- Alvesson, M. (2003). Beyond Neopositivists, Romantics, and Localists: A Reflexive Approach to Interviews in Organizational Research. *The Academy of Management Review*, 28(1), 13-33.
- Ang, J. S. (1991). Small business uniqueness and the theory of financial management. *Journal of Small Business Finance*, 1(1), 1-13.
- Ang, J. S. (1992). On the Theory of Finance for Privately Held Firms. *Journal of Small Business Finance*, 1(3), 185-203.
- Ardalan, K. (2008). *On the Role of Paradigms in Finance*. Hampshire: Ashgate Publications.
- Austin, T. J., Fox, M. A., & Hamilton, R. T. (1996). A study of small and medium sized business financing in New Zealand. Wellington: Ministry of Commerce.
- Avery, R. B., Bostic, R. W., & Samolyk, K. A. (1998). The role of personal wealth in small business finance. *Journal of Banking and Finance*, 22(6), 1019-1061.
- Ayyagari, M., Demirgüç-Kunt, A., & Maksimovic, V. (2010). Formal versus informal finance: Evidence from China. *Review of Financial Studies*, 23(8), 3048-3097.
- Baas, T., & Schrooten, M. (2006). Relationship Banking and SMEs: A Theoretical Analysis. *Small Business Economics*, 27, 127-137.
- Bakos, Y., & Brynjolfsson, E. (1999). Bundling Information Goods: Pricing, Profits, and Efficiency. *Management Science*, 45(12), 1613-1630.
- Bartelsman, E., Stefano, S., & Fabiano, S. (2003). *Comparative analysis of firm demographics and survival: Micro-level evidence for the OECD countries*. Working Paper No 348. Economics Department. Organisation for Economic Co-operation and Development. Paris. Retrieved from <http://www.oecd.org/dataoecd/28/53/2494036.pdf>
- Basel Committee on Banking Supervision. (2000). Principles for the Management of Credit Risk (pp. 30).
- Basit, T. (2003). Manual or electronic? The role of coding in qualitative data analysis. *Educational Research*, 45(2), 143-154.
- Bass, D., & Rozario, B. (2011). *The Essential Guide to Credit Management and Debt Recovery in Hong Kong, Singapore and Malaysia*. Hong Kong: Sweet and Maxwell Asia.
- Bazeley, P. (2007). *Qualitative Data Analysis With NVivo*: Sage.
- Berger, A. N. (1999). *The 'Big Picture' of relationship finance in "Business Access to Capital and Credit"*. Paper presented at the Federal Reserve System Research Conference.



- Berger, A. N., Klapper, L. F., & Udell, G. F. (2001). The ability of banks to lend to informationally opaque small businesses. *Journal of Banking & Finance*, 25(12), 2127-2167.
- Berger, A. N., & Udell, G. F. (1995). Relationship Lending and Lines of Credit in Small Firm Finance. *The Journal of Business*, 68(3), 351-381.
- Berger, A. N., & Udell, G. F. (1998). The economics of small business finance: The roles of private equity and debt markets in the financial growth cycle. *Journal of Banking & Finance*, 22(6-8), 613-673.
- Berger, A. N., & Udell, G. F. (2002). Small business credit availability and relationship lending: the importance of bank organisational structure. *The Economic Journal*, 112(477), F32-F53.
- Berger, A. N., & Udell, G. F. (2003). Small Business and Debt Finance. In J. A. Zoltan & D. B. Audretsch (Eds.), *Handbook of Entrepreneurship Research An Interdisciplinary Survey and Introduction*: Kluwer Academic Publishers.
- Berger, A. N., & Udell, G. F. (2006). A more complete conceptual framework for SME finance. *Journal of Banking & Finance*, 30(11), 2945-2966.
- Berlin, M., & Mester, L. J. (1999). Deposits and relationship lending. *Review of Financial Studies*, 12(3), 579-607. doi: 10.1093/rfs/12.3.579
- Bettner, M. S., Robinson, C., & McGoun, E. (1994). The Case for Qualitative Research in Finance. *International Review of Financial Analysis*, 3(1), 1-18.
- Bharath, S., Dahiya, S., Saunders, A., & Srinivasan, A. (2007). So what do I get? The bank's view of lending relationships. *Journal of Financial Economics*, 85(2), 368-419.
- Bhattacharya, S., & Chiesa, G. (1995). Proprietary Information, Financial Intermediation, and Research Incentives. *Journal of Financial Intermediation*, 4(4), 328-357.
- Billett, M., Flannery, M., & Garfinkel, J. (1995). The effect of lender identify on a borrowing firm's equity return. *Journal of Finance*, 50, 699-718.
- Binks, M., Ennew, C., & Mowlah, A. (2006). The relationship between private businesses and their banks. *International Journal of Bank Marketing*, 24(5), 346 - 355.
- Birley, S., & Westhead, P. (1994). A taxonomy of business start-up reasons and their impact on firm growth and size. *Journal of Business Venturing*, 9(1), 7-31.
- Blaug, M. (1980). *The methodology of economics, or, how economists explain*: Cambridge University Press.
- Blumer, H. (1956). Sociological Analysis and the "Variable". *American Sociological Review*, 21(6), 683-690.
- Bogdan, R., & Biklen, S. K. (1992). *Qualitative research for education: An introduction to theory and methods*: Allyn and Bacon.
- Boot, A. (2000). Relationship Banking: What Do We Know? *Journal of Financial Intermediation*, 9, 7-25.
- Boot, A., & Thakor, A. V. (1994). Moral Hazard and Secured Lending in an Infinitely Repeated Credit Market Game. *International Economic Review*, 35(4), 899-920.
- Borrmann, G., & Tripe, D. (2008). *A Survey of Small Business Finance in New Zealand*. Paper presented at the 12th New Zealand Finance Colloquium, Whararata, Massey University, Palmerston North Campus, New Zealand. <http://www.nzfc.ac.nz/archives/2008/programme.html>

- Boulanouar, Z. (2003). *Financing Small Businesses: Does The Loan Officer To Small Business Owner Relationship Count? Japan: An Exploratory Study*. Masters, Hiroshima University, Hiroshima.
- Boulanouar, Z., & Locke, S. (2009). Cost of small business banking: A New Zealand study. *Service Business*, 3(3), 211-227.
- Boyatzis, R. E. (1998). *Transforming Qualitative Information: Thematic Analysis and Code Development*: Sage Publications.
- Braun, V., & Clarke, V. (2006). Using thematic analysis in psychology. *Qualitative Research in Psychology*, 3(2), 77-101.
- Britan, G. M. (1978). Experimental and contextual models of program evaluation. *Evaluation and Program Planning*, 1(3), 229-234. doi: 10.1016/0149-7189(78)90077-0
- Brown, M., & Zehnder, C. (2007). Credit Reporting, Relationship Banking, and Loan Repayment. *Journal of Money, Credit and Banking*, 39(8), 1883-1918.
- Bryman, A. (1988). *Quantity and quality in social research*: Unwin Hyman.
- Burke, A. E., FitzRoy, F. R., & Nolan, M. A. (2002). Self-employment wealth and job creation: The roles of gender, non-pecuniary motivation and entrepreneurial ability. *Small Business Economics*, 19(3), 255-270.
- Burton, B. (2007). Qualitative research in finance – pedigree and renaissance. *Studies in Economics and Finance*, 24(1), 5-12.
- Cameron, K. S., & Quinn, R. E. (1988). Organizational Paradox and Transformation. In R. E. Quinn & K. S. Cameron (Eds.), *Paradox and Transformation: Toward a Theory of Change in Organization and Management*. Cambridge: Ballinger Publishing Co.
- Cameron, L., Chapple, B., Davis, N., Kousis, A., & Lewis, G. (2007). *New Zealand Financial Markets, Saving and Investment*. New Zealand Treasury Policy Perspectives Paper 07/01.
- Casu, B., Girardone, C., & Molyneux, P. (2006). *Introduction to Banking*: Prentice Hall.
- Chan, D., Schumacher, C., & Tripe, D. (2007). *Bank Competition in New Zealand and Australia*. Paper presented at the 12th Finsia-Melbourne Centre for Financial Studies Banking and Finance Conference, Melbourne, 24-25 September 2007.
- Charmaz, K. (2002). Qualitative interviewing and grounded theory analysis. In J. F. Gubrium & J. A. Holstein (Eds.), *Handbook of interview research: Context & method* (pp. 675-684). Thousand Oaks, CA: Sage.
- Cole, A. R. (1998). The importance of relationships to the availability of credit. *Journal of Banking & Finance*, 22, 959-977.
- Coleman, S. (2008). *The Determinants of Capital Structure in Small Firms: New Evidence from the 2003 Survey of Small Business Finance*. Paper presented at the International Council for Small Business World Conference, Halifax, Nova Scotia, Canada.
- Colgate, M., & Lang, B. (2005). Positive and negative consequences of a relationship manager strategy: New Zealand banks and their small business customers. *Journal of Business Research*, 58(2), 195-204. doi: 10.1016/s0148-2963(02)00494-0
- Colgate, M., & Norris, M. (2001). Developing a Comprehensive Picture of Service Failure. *International Journal of Service Industry*, 12(3/4), 215-234.

- Collins, O. F., & Moore, D. G. (1970). *The Organisation Makers*. New York: Appleton Century Crofts.
- Cooper, H. M. (1984). *The integrative research review: a systematic approach*: Sage Publications.
- Corbin, J. M., & Strauss, A. L. (2008). *Basics of Qualitative Research: Techniques and Procedures for Developing Grounded Theory* (3 ed.): Sage Publications.
- Corman, J., Pennel, L., & Lussier, R. (2008). *Small business management: A Planning Approach* (3rd ed.): Atomic Dog.
- Cromie, S. (1987). Motivations of aspiring male and female entrepreneurs. *Journal of Organizational Behavior*, 8(3), 251-261.
- Culkin, N., & Smith, D. (2000). An emotional business: A guide to understanding the motivations of small business decision takers. *Qualitative Market Research*, 3(3), 145-157.
- Curran, J. (1986). *Bolton fifteen years on: A review and analysis of small business research in Britain 1971–1986*. London: Small Business Research Trust.
- Daley, B. J. (2004). *using concept maps in qualitative research*. Paper presented at the the first international conference on Concept Mapping, Pamplona, Spain.
- Daly, J., Kellehear, A., & Gliksman, M. (1997). *The public health researcher: A methodological approach*. Melbourne, Australia: Oxford University Press.
- De Haas, R., Ferreira, D., & Taci, A. (2010). What determines the composition of banks' loan portfolios? Evidence from transition countries. *Journal of Banking and Finance*, 34(2), 388-398.
- Deakins, D., & Hussain, G. (1994). Risk Assessment with Asymmetric Information. *International Journal of Bank Marketing*, 12(1), 24 - 31.
- Degryse, H., & Cayseele, P. V. (2000). Relationship lending within a bank-based system: evidence from European small business data. *Journal of Financial Intermediation*, 9, 90-109.
- Denscombe, M. (2007). *The Good Research Guide for small-scale social research projects* (3rd edition ed.): Open University Press.
- Denzin, N. K., & Lincoln, Y. S. (1994). *Handbook of qualitative research*: Sage Publications.
- Dey, I. (1993). *Qualitative Data Analysis: A User-Friendly Guide for Social Scientists*. New York: Routledge.
- Diamond, D. W. (1991). Debt maturity structure and liquidity risk. *Quarterly Journal of Economics*, 106(3), 709-737.
- Diamond, D. W., & Dybvig, P. H. (1983). Bank Runs, Deposit Insurance, and Liquidity. *Journal of Political Economy*, 91(3), 401-419.
- Dorfman, R. (2007). 4 small-business success strategies. *ABA Bank Marketing*, 39, 24–29.
- Duarte, F., & Gama, A. P. (2011, 9-10 November). *The Role of Collateral and Relationship lending in loan pricing: evidence from United Kingdom SMEs*. Paper presented at the ISBE, Sheffield, UK.
- Duncan, M., & Jason, T. (2004). *Firm Dynamics in New Zealand: A Comparative Analysis with OECD Countries*. New Zealand Treasury Working Paper 04/11.
- Easterby-Smith, M., Thorpe, R., & Lowe, A. (2002). *Management Research: An Introduction*: Sage Publications.

- Edelman Trust Barometer. (2012). Financial Sector Least Trusted. Retrieved from <http://trust.edelman.com/trusts/trust-in-institutions-2/financial-sector-least-trusted/>
- Eisenhardt, K. M. (1989). Building Theories from Case Study Research. *The Academy of Management Review*, 14(4), 532-550.
- Elsas, R. (2005). Empirical determinants of relationship lending. *Journal of Financial Intermediation*, 14(1), 32-57.
- Enrich, D. (2007). Banks court small businesses, *Wall Street Journal*, April 11.
- Ergungor, O. E. (2005). The profitability of bank–borrower relationships. *Journal of Financial Intermediation*, 14(4), 485-512. doi: 10.1016/j.jfi.2004.09.002
- Erickson, F. (1986). Qualitative methods on research on teaching. In M. Wittrock (Ed.), *Handbook of research on teaching* (3rd ed., pp. 119–161). New York: Macmillan.
- Ernst & Young. (2009). Talking SMEs: Ernst & Young.
- Ernst & Young. (2011). Ernst & Young Global Consumer Banking Survey A new era of customer expectation: Ernst & Young.
- Evans, L., Grimes, A., & Wilkinson, B. (1996). Economic Reform in New Zealand 1984-95: The Pursuit of Efficiency. *Journal of Economic Literature*, 34(4).
- Fama, E. F. (1985). What's Different about Banks? *Journal of Monetary Economics*, 15(January), 29-39.
- Fereday, J., & Muir-Cochrane, E. (2006). Demonstrating Rigor Using Thematic Analysis: A Hybrid Approach of Inductive and Deductive Coding and Theme Development. *International Journal of Qualitative Methods*, 5(1), 80-92.
- Fielding, N., & Fielding, J. L. (1986). *Linking data*: Sage Publications.
- Fisher, A. (2001). Winning the Battle for Customers. *Journal of Financial Services Marketing*, 6(1, September), 77-84.
- Flick, U. (2002). *An introduction to qualitative research*: Sage.
- Flyvbjerg, B. (2006). Five Misunderstandings About Case-Study Research. *Qualitative Inquiry*, 12(2), 219-245. doi: 10.1177/1077800405284363
- Foss, S., K., & Waters, W. (2003). Coding & Analysis of Qualitative Data. Retrieved from <http://www.abdsurvivalguide.com/News/020603.htm> website:
- Frankfurter, G. M., Carleton, W., Gordon, M., Horrigan, J., McGoun, E., Philippatos, G., & Robinson, C. (1994). The methodology of finance: A round table discussion. *International Review of Financial Analysis*, 3(3), 173-207.
- Freixas, X. (2005). Deconstructing relationship banking. *Investigaciones Economicas*, 29(1), 3-31.
- Freixas, X., & Rochet, J.-C. (1997). *Microeconomics of Banking*: MIT Press.
- Freixas, X., & Rochet, J.-C. (2008). *Microeconomics of Banking* (second ed.): MIT Press.
- Gan, C., Cohen, D., Clemes, M., & Chong, E. (2006). A Survey of Customer Retention in the New Zealand Banking Industry. *Banks and Bank Systems*, 1(4).
- Geertz, C. (1973). COMMENTS ON WHITE,B DEMAND FOR LABOR AND POPULATION GROWTH IN COLONIAL-JAVA. [Article]. *Human Ecology*, 1(3), 237-239. doi: 10.1007/bf01531183
- Gehr, A. K. (1979). Risk and Return. *The Journal of Finance*, 34(4), 1027-1030. doi: 10.1111/j.1540-6261.1979.tb03455.x

- George, A. L., & Bennett, A. (2005). *Case Studies And Theory Development In The Social Sciences*: Mit Press.
- Gibbs, G. R. (2008). *Analysing Qualitative Data*: Sage.
- Gibson, B. (2001). *Financial structures in Australian small firms*. Department of accounting and finance working papers. The university of Newcastle. NSW.
- Gill, A. S., Flaschner, A. B., & Shachar, M. (2006). Factors that affect the trust of business clients in their banks. *International Journal of Bank Marketing*, 24(6), 384-405.
- Gray, J. (1994). *Unemployment to Entrepreneurship: Conditions that Launch Redundant Workers into Self-employment*. Paper presented at the ANZAM conference, Victoria: Monash University.
- Greenbaum, S. I., Kanatas, G., & Venezia, I. (1989). Equilibrium loan pricing under the bank-client relationship. *Journal of Banking & Finance*, 13(2), 221-235. doi: 10.1016/0378-4266(89)90061-7
- Greenbaum, S. I., & Thakor, A. V. (2007). *Contemporary Financial Intermediation* (second ed.): Academic press.
- Gregory, B. T., Rutherford, M. W., Oswald, S., & Gardiner, L. (2005). An Empirical Investigation of the Growth Cycle Theory of Small Firm Financing. *Journal of Small Business Management*, 43(4), 382-392. doi: 10.1111/j.1540-627X.2005.00143.x
- Grimes, A. (1998). Liberalisation of financial markets in New Zealand. *Reserve Bank of New Zealand Bulletin*, 61.
- Guo, S., Cockburn-Wooten, C., & Simpson, M. (2008, 9-11 July). *The socialisation processes of 'Asian-bringing employees' in the New Zealand banking industry*. Paper presented at the Australian and New Zealand Communication Association Conference, Wellington, New Zealand.
- Gurley, J. G., & Shaw, E. S. (1960). *Money in the Theory of Finance*. Washington: Brookings Institution.
- Hamilton, R. T. (1987). Motivations and Aspirations of Business Founders. *International Small Business Journal*, 6(1), 70-78.
- Han, L., & Greene, F. (2007). The determinants of online loan applications from small businesses. [DOI: 10.1108/14626000710773556]. *Journal of Small Business and Enterprise Development*, 14(3), 478-486.
- Heffernan, S. (2005). *Modern banking*: Wiley.
- Hess, K. (2008). *Credit Loss Dynamics in Australasian Banking*. PhD PhD, University of Waikato, Hamilton, New Zealand. Retrieved from <http://adt.waikato.ac.nz/public/adt-uow20080415.160649/index.html>
- Hodgman, D. R. (1961). The Deposit Relationship and Commercial Bank Investment Behavior. *The Review of Economics and Statistics*, 43(3), 257-268.
- Holmes, S., Hutchinson, P., Gibson, B., Forsaith, D., & McMahon, R. (2003). *Small enterprise finance*: John Wiley & Sons.
- Hoshi, T., Kashyap, A., & Scharfstein, D. (1990). The role of banks in reducing the costs of financial distress in Japan. *Journal of Financial Economics*, 27, 67-88.
- Infometrics Ltd. (2004). New Zealand's Angel Capital Market: the supply side: For Ministry of Economic Development.

- Irwin, D., & Scott, J. M. (2010). Barriers faced by SMEs in raising bank finance. *International Journal of Entrepreneurial Behaviour & Research*, 16(3), 245 - 259.
- Jarvis, R. (2000). Finance and the small firm. In S. Carter & D. Jones-Evans (Eds.), *Enterprise and Small Business: Principles, Practice and Policy*. London: FT Prentice Hall.
- Joffe, H., & Yardley, L. (2004). Content and thematic analysis. In D. F. Marks & L. Yardley (Eds.), *Research Methods for Clinical and Health Psychology* (pp. 56-68). London: Sage.
- Johnson, P., Curran, J., Duberley, J., & Blackburn, R. A. (2001). *Researching the Small Enterprise*: Sage Publications.
- Jones, S. (1985). Depth interviewing. In R. Walker (Ed.), *Applied Qualitative Research* (pp. 45-55): Gower Publications.
- Kamakura, W. A., Wedel, M., de Rosa, F., & Mazzon, J. A. (2003). Cross-selling through database marketing: a mixed data factor analyzer for data augmentation and prediction. *International Journal of Research in Marketing*, 20(1), 45-65.
- Keasey, K., & Watson, R. (1993). *Small Firm Management: Ownership, Finance and Performance*: Wiley-Blackwell.
- King, N. (1994). The Qualitative Research Interview. In C. Cassel & G. Symon (Eds.), *In Qualitative methods in organizational research: A practical guide* (pp. 14-34). London: Sage Publications.
- Koch, T. W., & MacDonald, S. S. (2009). *Bank Management*: Cengage Learning.
- KPMG. (2013). Financial Institutions Performance Survey Review 2012: A solid base - now onwards and upwards?
- Kuzel, A. J. (1999). Sampling in Qualitative Inquiry. In B. F. Crabtree & W. L. Miller (Eds.), *Doing Qualitative Research* (pp. 33-45). Thousand Oaks, CA: Sage Publications.
- Kvale, S. (2007). *Doing Interviews*: Sage publications.
- Kvale, S., & Brinkmann, S. (2009). *InterViews: Learning the Craft of Qualitative Research Interviewing*: Sage Publications.
- Lave, C. A., & March, J. G. (1975). *An Introduction to Models in the Social Sciences*. New York: Harper & Row.
- LeCornu, M. R., McMahon, R. G. P., Forsaith, D. M., & Stanger, A. M. J. (1996). The small enterprise financial objective function: An exploratory study. *Journal of Small Business Management*, 34(3), 1-14.
- Leland, H. E., & Pyle, D. H. (1977). Informational Asymmetries, Financial Structure, and Financial Intermediation. *The Journal of Finance*, 32(2), 371-387.
- Lewins, A., & Silver, C. (2007). *Using Software in Qualitative Research: A Step-By-Step Guide*: Sage.
- Locke, S., & Drever, M. (2008). *Why Do Small Business Owner-Managers Choose Particular Banks*. Paper presented at the International Council for Small Business World Conference, Halifax, Nova Scotia, Canada.
- Lucas, L. M., & Davis, M. (2005). The Role of the banker-small business owner network in inner-city lending. *Journal of Applied Management and Entrepreneurship*, 10(3), 3-20.
- Lucey, A. J. (1990). What bank services do small businesses want? *Commer Lend Rev*, 5(3), 92.

- Lummer, S., & McConnell, J. (1989). Further evidence on the bank lending process and the capital market response to bank loan agreements. *Journal of Financial Economics*, 25, 99-122.
- Mackintosh, J. (2001). Banking competition “limited by enterprises favouring branches”, *Financial Times*.
- MacQueen, K., McLellan-Lemal, E., Bartholow, K., & Milstein, B. (2008). Team-based codebook development: Structure, process, and agreement. In G. Guest & K. M. MacQueen (Eds.), *Handbook for team-based qualitative research* (pp. 119-135). Lanham, MD: AltaMira.
- Malik, S. H., & Coulson, N. (2008). Computer-mediated infertility support groups: An exploratory study of online experiences. *Patient Education and Counseling*, 73, 105-113.
- Mann, R. J. (1998). Comment on Avery, Bostic and Samolyk. *Journal of Banking and Finance*, 22(6), 1062-1066.
- Maque, I. (2007). *Les relations bancaires d'une entreprise: fonctionnement et organisation une application a la PME*. PhD, University of Monteaquieu-Bordeaux IV, Bordeaux.
- Mason, C., & Pinch, S. (1991). Self-employment in a British city: An analysis of household survey data. *International Small Business Journal*, 19(1), 27-43.
- Mason, J. (1996). *Qualitative researching*. London: Sage Publications.
- Mason, J. (2002). *Qualitative Researching*: Sage Publications.
- Matthews, C. D. (2009). *Switching Costs in the New Zealand Banking Market*. PhD, Massey University, Palmerston North, New Zealand.
- Matthews, K., & Thompson, J. (2008). *The Economics of Banking*. West Sussex: Wiley.
- Maxwell, J. A. (2004a). Causal Explanation, Qualitative Research, and Scientific Inquiry in Education. *Educational Researcher*, 33(2), 3-11. doi: 10.3102/0013189x033002003
- Maxwell, J. A. (2004b). Using Qualitative Methods for Causal Explanation. *Field Methods*, 16(3), 243-264. doi: 10.1177/1525822x04266831
- Maxwell, J. A. (2005). *Qualitative Research Design: An Interactive Approach* (2nd ed.): Sage Publications.
- Maxwell, J. A. (2012). *A Realist Approach for Qualitative Research*: Sage Publications.
- Maxwell, J. A., & Loomis, D. M. (2003). Mixed Methods Design: An Alternative Approach. In A. Tashakkori & C. Teddlie (Eds.), *Handbook of Mixed Methods in Social and Behavioral Research* (pp. 209-240): Thousand Oaks, CA: Sage.
- Mazur, M. (2007). Bank products lack differentiation in eyes of small business owners. *Community Banker*, 16, 66.
- McGoun, E. G. (2003). Special issue: alternative perspectives in finance. *International Review of Financial Analysis*, 12(4), 347. doi: 10.1016/s1057-5219(03)00029-2
- McMahon, R., & Holmes, S. (1989). small business financial management: an international review of practice. Adelaide: University of Flinders.
- McMillan, J. (1998). Managing Economic Change: Lessons from New Zealand. *World Economy*, 21(6), 827-843. doi: 10.1111/1467-9701.00165



- Merriam, S. B. (1988). *Case Study Research in Education: A Qualitative Approach*. San Francisco: Jossey-Bass.
- Merton, R. C. (1995). A Functional Perspective of Financial Intermediation. *Financial Management*, 24(summer), 23-41.
- Miles, M. B., & Huberman, A. M. (1984). *Qualitative data analysis: a sourcebook of new methods*: Sage Publications.
- Miles, M. B., & Huberman, A. M. (1994). *Qualitative Data Analysis: An Expanded Sourcebook*: Sage Publications.
- Mills, D. (2003). Firm performance. *Growth Seminar Series* [Presentation to the Treasury/Ministry of Economic Development]. Wellington: New Zealand Treasury.
- Minh To, H., & Tripe, D. (2002). Factors influencing the performance of foreign-owned banks in New Zealand. *Journal of International Financial Markets, Institutions and Money*, 12(4-5), 341-357. doi: 10.1016/s1042-4431(02)00018-5
- Ministry of Economic Development. (2003a). *Bank Lending Practices to Small and Medium Sized Enterprises*.
- Ministry of Economic Development. (2003b). SMEs in New Zealand: Structure and Dynamics 2003.
- Ministry of Economic Development. (2005). *Business finance in New Zealand 2004*. Retrieved from <http://www.stats.govt.nz/publications/businessfinancialandstructural/business-finance-nz-2004.aspx>.
- Ministry of Economic Development. (2010). *SMEs in New Zealand: Structure and Dynamics 2010*. Ministry of Economic Development Retrieved from <http://www.med.govt.nz/upload/74417/SMEs%20in%20New%20Zealand%20Structure%20and%20Dynamics%202010.pdf>.
- Ministry of Economic Development. (2011). SMEs in New Zealand: Structure and Dynamics 2011.
- Mohr, L. B. (1982). *Explaining Organizational Behavior* (1st ed.): Jossey-Bass.
- Morse, J. (1994). Emerging from the Data: Cognitive Processes of Analysis in Qualitative Research. In J. Morse (Ed.), *Critical Issues in Qualitative Research Methods* (pp. 23-41). Thousand Oaks, CA: Sage
- Myers, M. D. (1997). Qualitative Research in Information Systems. *Management Information Systems Quarterly*, 21(2), 241 – 242.
- Nakamura, L. I. (1993). Commercial bank information: Implications for the structure of banking. In a. L. W. M. Klausner (Ed.), *Structural Change in Banking* (pp. 131-160): Homewood, IL: Irwin.
- Namey, E., Guest, G., Thairu, L., & Johnson, L. (2008). Data Reduction Techniques for Large Qualitative Data Sets. In G. Guest & K. M. MacQueen (Eds.), *Handbook for team-based qualitative research* (pp. 137-163). Lanham, MD: AltaMira.
- New Zealand Bankers' Association. (1997). Getting it Right: A Guide to Banking. In NZBA (Ed.), (second ed.).
- New Zealand Bankers' Association. (2006). Banking in New Zealand. In NZBA (Ed.), (Fourth ed.).



- Niskanen, M., & Niskanen, J. (2010). Small Business Borrowing and the Owner–Manager Agency Costs: Evidence on Finnish Data. *Journal of Small Business Management*, 48(1), 16-31.
- Novak, J. D., & Gowin, D. B. (1984). *Learning How to Learn*: Cambridge University Press.
- NRC, C. o. S. P. f. E. R. N. R. C. (2002). *Scientific Research in Education*: The National Academies Press.
- O'Connor, J. (1983). Issues in enterprise development: Business owners perceptions and experiences. *Irish Journal of Business and Administrative Research*, 4, 31-43.
- OECD. (2004). SME Statistics: Towards a More Systematic Statistical Measurement of SME Behaviour. Background report for the 2nd OECD Conference of Ministers Responsible for Small and Medium Enterprises: OECD.
- OECD. (2006). *The SME Financing Gap (Vol. I) Theory and Evidence*: OECD Publishing.
- Ongena, S., & Smith, D. C. (2000). Bank Relationships: A Review. In P. Harker & S. A. Zenios (Eds.), *The Performance of Financial Institutions* (pp. 221-258): Cambridge University Press.
- Orlikowski, W. J., & Baroudi, J. J. (1991). Studying Information Technology in Organizations: Research Approaches and Assumptions. *Information Systems Research*, 2(1), 1-28. doi: 10.1287/isre.2.1.1
- Osland, G. E., & Cavusgil, S. T. (1998). The use of multiple-party perspectives in international joint venture research. *Management International Review*, 38(3), 191-202.
- Owen, W. F. (1984). Interpretive themes in relational communication. *Quarterly Journal of Speech*, 70, 274-287.
- Palys, T. S. (2008). Purposive sampling. In L. M. Given (Ed.), *The Sage Encyclopedia of Qualitative Research Methods* (Vol. 2, pp. 697-698). Thousand oaks, CA: Sage Publications.
- Patton, M. Q. (1990). *Qualitative evaluation and research methods*: Sage Publications.
- Pawson, R., & Tilley, N. (1997). *Realistic Evaluation*: Sage.
- Peltoniemi, J. (2007). The Benefits of Relationship Banking: Evidence from Small Business Financing in Finland. *Journal of Financial Services Research*, 31(2), 153-171.
- Perry, M., Cardow, A., Massey, C., & Tweed, D. (2006). *Telling tales: a report on New Zealand SMEs & their relationships with banks & accountants*. Paper presented at the The fourth symposium of the New Zealand Centre for SME Research: The people behind the profit, Wellington , New Zealand : NZ Centre for SME Research, Massey University. <http://sme-centre.massey.ac.nz/staff.asp?id=1>
- Petersen, M. A. (2004). *Information: Hard and soft*. Working paper. Kellogg School of Management, Northwestern University.
- Petersen, M. A., & Rajan, R. G. (1994). The Benefits of Lending Relationships: Evidence from Small Business Data. *Journal of Finance*, 49(1), 3-37.
- Puri, M., Rocholl, J., & Steffen, S. (2011). On the importance of prior relationships in bank loans to retail customers: European Central Bank.

- Qu, S. Q., & Dumay, J. (2011). The qualitative research interview. [DOI: 10.1108/11766091111162070]. *Qualitative Research in Accounting & Management*, 8(3), 238-264.
- Ragin, C. C. (1989). *The Comparative Method: Moving Beyond Qualitative and Quantitative Strategies* University of California Press
- Rajan, R., & Winton, A. (1995). Covenants and Collateral as Incentives to Monitor. *The Journal of Finance*, 50(4), 1113-1146.
- Ramakrishnan, R. T. S., & Thakor, A. V. (1985). Information Reliability and a Theory of Financial Intermediation. *Review of Economic Studies*, 51(July), 415-432.
- Reddy, M. (2007). Small business in small economies: constraints and opportunities for growth. *Social and Economic Studies*, 56(1 & 2), 304-321.
- Reichheld, F. F. (1996). Learning from Customer Defections. *Harvard Business Review*, March/April, 56-69.
- Reserve Bank of New Zealand. (1986). Financial Policy Reform. Wellington.
- Reserve Bank of New Zealand. (2012). Register of registered banks in New Zealand Retrieved from <http://www.rbnz.govt.nz/nzbanks/0091622.html> website: <http://www.rbnz.govt.nz/nzbanks/0091622.html>
- Rice, P., & Ezzy, D. (1999). *Qualitative research methods: A health focus*. Melbourne, Australia: Oxford University Press.
- Richards, L., & Morse, J. M. (2007). *Readme First for a User's Guide to Qualitative Methods*: Sage Publications.
- Roberts, E. B., & Wainer, H. A. (1971). Some characteristics of technical entrepreneurs. *I.E. E. Transactions on Engineering Management*, 18, 100-109.
- Robertson, B., & Belanger, B. (2006). *Building a Better Understanding of SME Financing: Lessons learnt by Canada and New Zealand on SME Finance Data Collection Initiatives*. Paper presented at the The SME financing gap, Brasilia.
- Rosen, M. (1991). COMING TO TERMS WITH THE FIELD: UNDERSTANDING AND DOING ORGANIZATIONAL ETHNOGRAPHY\*. *Journal of Management Studies*, 28(1), 1-24. doi: 10.1111/j.1467-6486.1991.tb00268.x
- Rossmann, G. B., & Rallis, S. F. (2003). *Learning in the Field: An Introduction to Qualitative Research*: Sage Publications.
- Saldaña, J. (2009). *The coding manual for qualitative researchers*: Sage.
- Sayer, R. A. (2000). *Realism and Social Science*: Sage.
- Scheinberg, S., & MacMillan, I. C. (1988). An eleven country study of motivations to start a business. In B. A. Kirchoff, W. A. Long, W. E. McMullan, K. H. Vesper & W. E. J. Wetzels (Eds.), *Frontiers of Entrepreneurship Research* (pp. 669-687). Wellesley, MA: Babson College.
- Schwandt, T. A. (1997). *Qualitative inquiry: a dictionary of terms*: Sage Publications.
- Scott, J., & Dunkelberg, B. (2006). Convenient location most important bank characteristic according to small business owners. *Business Credit*, 108, 41.
- Scott, J. A. (2006). Loan Officer Turnover and Credit Availability for Small Firms. *Journal of Small Business Management*, 44(4), 544.
- Sharpe, S. A. (1990). Asymmetric Information, Bank Lending and Implicit Contracts: A Stylized Model of Customer Relationships. *The Journal of Finance*, 45(4), 1069-1087.

- Shen, Y. (2007). *The happy story told by small business capital structure*. Master thesis, Waikato University, Hamilton, New Zealand.
- Silverman, D. (2005). *Doing Qualitative Research: A Practical Handbook*: Sage.
- Silverman, D. (2009). *Doing Qualitative Research*: Sage.
- Singh, G., & DeNoble, A. (2003). Early retirees as the next generation of entrepreneurs. *Entrepreneurship Theory and Practice*, 27(3), 207-226.
- Slovin, M. B., Sushka, M. E., & Poloncheck, J. A. (1993). The value of bank durability: Borrowers as bank stakeholders., . *Journal of Finance*, 48, 247-266.
- Smallbone, D., & Wyer, P. (2000). Growth and Development in the Small Firms. In S. Carter & D. Jones-Evans (Eds.), *Enterprise and Small Business: Principles, Practice and Policy* (pp. 409-433). Harlow: Financial Times Prentice Hall.
- Smith, R., & Tripe, D. (2001). *Competition and Constestability in New Zealand's Banking System*. Paper presented at the 14th Australasian Finance and Banking Conference, University of New South Wales.
- Stake, R. E. (2005). Qualitative case studies. In N. K. Denzin & Y. S. Lincoln (Eds.), *The SAGE handbook of qualitative research* (3rd ed., pp. 443-466). Thousand Oaks, CA: SAGE.
- Stanworth, J., & Curran, J. (1973). *Managemenet Motivation in the Smaller Business*. Essex: Gower.
- Statistics New Zealand. (2004). Business finance in New Zealand 2004. Wellington.
- Stein, J. C. (2002). Information production and capital allocation: Decentralized versus hierarchical firms. *Journal of Finance*, 57(5), 1891-1921.
- Stiglitz, J. E., & Weiss, A. (1981). Credit Rationing in Markets with Imperfect Information. *American Economic Review*, 71(3), 393.
- Storey, D. J. (1982). *Entrepreneurship and the New Small Firm*. Kent, UK: Croom Helm.
- Storey, D. J. (1994). *Understanding the Small Business Sector*. New York: Routledge.
- Strauss, A. L., & Corbin, J. M. (1998). *Basics of Qualitative Research: Techniques and Procedures for Developing Grounded Theory*: Sage Publications.
- Taketa, K., & Udell, G. F. (2007). Lending Channels and Financial Shocks: The Case of SME Trade Credit and the Japanese Banking Crisis. *Monetary and Economic Studies*, November.
- Taylor, C., & Gibbs, G. R. (2010). How and what to code. Retrieved from How and what to code website:  
onlineqda.hud.ac.uk/Intro\_QDA/how\_what\_to\_code.php
- Tesch, R. (1990). *Qualitative Research: Analysis Types and Software Tools*: Falmer Press.
- Thakor, A. V. (1995). Financial Intermediation and the Market for Credit In R. A. Jarrow, V. Maksimovic & W. T. Ziemba (Eds.), *Finance* (Vol. 9, pp. 1073-1103). Amsterdam: Elsevier.
- Thomas, G. (2011). A Typology for the Case Study in Social Science Following a Review of Definition, Discourse, and Structure. *Qualitative Inquiry*, 17(6), 511-521. doi: 10.1177/1077800411409884
- Tripe, D. (2004). *The New Zealand Banking System and the Balance of Payments*. Paper presented at the Paper for 8th New Zealand Finance Colloquium, Hamilton.

- Tripe, D. (2007). *The relative efficiency of banks, taking into account a customer satisfaction rating*. Paper presented at the 20th Australasian Banking and Finance Conference, Sydney, December.
- Tripe, D. (2009). *New Zealand and the Financial Crisis of 2008*. Workshop. Reserve Bank of New Zealand. Retrieved from <http://www.rbnz.govt.nz/research/workshops/june2009/3732339.pdf>
- Uchida, H., Udell, G. F., & Watanabe, W. (2006). Bank Size and Lending Relationships in Japan," [Discussion papers 06029]. *Research Institute of Economy, Trade and Industry*.
- Udell, G. F. (1989). Loan quality, commercial loan review and loan officer contracting. *Journal of Banking & Finance*, 13(3), 367-382. doi: 10.1016/0378-4266(89)90048-4
- Udell, G. F. (2008). What's in a relationship The case of commercial lending. [Featured Articles]. *Business Horizons*, 51(2), 93-103.
- Uzzi, B. (1999). Embeddedness in the Making of Financial Capital: How Social Relations and Networks Benefit Firms Seeking Financing. *American Sociological Review*, 64(4), 481-505.
- Vass, B. (2009, December 3). Bank rejects big offices to get closer to customers, *NZ Herald*. Retrieved from [http://www.nzherald.co.nz/nz/news/article.cfm?c\\_id=1&objectid=10613084](http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=10613084)
- Vos, E., Yeh, A. J.-Y., Carter, S., & Tagg, S. (2007). The happy story of small business financing. *Journal of Banking & Finance*, 31(9), 2648-2672.
- Walker, E., & Brown, A. (2004). What Success Factors are Important to Small Business Owners? *International Small Business Journal*, 22(6), 577-594. doi: 10.1177/0266242604047411
- Walker, R. (1985). *Applied qualitative research*: Gower.
- Wallace, W. L. (1969). *Sociological theory*. London: Heinemann.
- Weiss, R. S. (1994). *Learning from strangers: the art and method of qualitative interview studies*: Free Press.
- Welsh, E. (2002). Dealing with Data: Using NVivo in the Qualitative Data Analysis Process. *Qualitative Social Research*, 3(2), 1-7., 3(2), 1-7.
- Whyte, W. F. (1982). Interviewing in field research. In R. G. Burgess (Ed.), *Field research: a sourcebook and field manual*. London: George Allen and Unwin.
- Wieviorka, M. (1992). Case studies: History or sociology? In C. C. Ragin & H. S. Becker (Eds.), *What is a case? Exploring the foundations of social inquiry* (pp. 159-172). New York: Cambridge University Press.
- Willig, C. (2001). *Introducing Qualitative Research in Psychology: Adventures in Theory and Method*: Open University Press.
- Yin, R. K. (1994). *Case study research: design and methods*: Sage Publications.
- Yin, R. K. (2003a). *Applications of case study research*: Sage Publications.
- Yin, R. K. (2003b). *Case Study Research: Design and Methods* (Third Edition ed. Vol. 5): Sage Publications, Inc.
- Yin, R. K. (2006). Case Study Methods. In J. L. Green, G. Camilli & P. B. Elmore (Eds.), *Handbook of Complementary Methods in Education Research* (3rd ed., pp. 111-122): Lawrence Erlbaum Associates.

## IX. Appendices

### IX.1 Appendix 1: Consent Form for Participants

#### *Consent Form for Participants*

**Waikato Management School**

Te Raupapa



THE UNIVERSITY OF  
**WAIKATO**  
*Te Whare Wānanga o Waikato*

#### *The Small Business-Bank Relationship In New Zealand:*

##### *Consent Form for Participants*

I have read the Information Sheet for Participants for this study and have had the details of the study explained to me. My questions about the study have been answered to my satisfaction, and I understand that I may ask further questions at any time.

I also understand that I am free to withdraw from the study at any time during the interview process, or to decline to answer any particular questions in the study. I agree to provide information to the researcher under the conditions of confidentiality set out on the Information Sheet.

I agree to participate in this study under the conditions set out in the Information Sheet form.

Signed: \_\_\_\_\_

Name: \_\_\_\_\_

Date: \_\_\_\_\_

Researcher's Name and contact information:

Zakaria Boulanouar, Department of Finance, University of Waikato Management School, Hamilton, New Zealand.

Phone: work: 07-838-4957 and mobile: 021-185-3173

Supervisors' Name and contact information:

⊕ Dr Stuart Locke; Department of Finance, University of Waikato Management School, Hamilton, New Zealand.

Phone: work: 07-838- 4756 and mobile: 021473073

⊕ Dr Mark Holmes; Department of Economics, University of Waikato  
Management School, Hamilton, New Zealand.  
Phone: work: 07-838-4454.

## IX.2 Appendix 2: The participant Information Sheet

Department of finance  
Waikato Management School  
The University of Waikato  
Private Bag 3105  
Hamilton, New Zealand

Telephone 64-7-838 4466 Extn. 4957  
Facsimile 64-7-838-4331  
[www.mngt.waikato.ac.nz/](http://www.mngt.waikato.ac.nz/)  
Email: [zakaria@mngt.waikato.ac.nz](mailto:zakaria@mngt.waikato.ac.nz)



### The participant Information Sheet

#### Overview

For my doctoral research in Finance, I'm conducting interviews of loan officers/relationship managers and bank managers concerning small business-bank relationships in New Zealand.

#### Who's responsible?

I am Zakaria Boulanouar, a doctoral research student in the University of Waikato Management School under the supervision of Drs Stuart Locke and Mark Holmes.

You can phone me at 07-838-4957, email me at [zakaria@mngt.waikato.ac.nz](mailto:zakaria@mngt.waikato.ac.nz) or contact me at the address on the letterhead.

You can also get in touch with either of my supervisors:

Dr Stuart Locke	Dr Mark Holmes
07-838-4756	07-838-4454
<a href="mailto:smlocke@waikato.ac.nz">smlocke@waikato.ac.nz</a>	<a href="mailto:holmesmj@waikato.ac.nz">holmesmj@waikato.ac.nz</a>

#### What's the research study about?

The study seeks to develop a model of risk and return components of small business relationship banking in New Zealand, investigating the following propositions as the project objectives:

- Relationship banking is an efficient process for reducing bank risks and increasing its return opportunities resulting from information asymmetry when dealing with small businesses.

- Banks use a trade-off approach between costs and benefits of the type of relationship banking for each parallel as an allocation mechanism of the degree of relationship banking intensity.
- Small and medium sized enterprises are sectioned into parallels/tranches according to some measures (turnover, growth capacity, transaction or fee levels, loan size...) and types of relationships banking are decided/allocated accordingly.

It is anticipated the study will contribute to a better understanding of how small business-bank relationships work, identifying the source(s) of value added by these types of relationships.

What will you have to do and how long will it take?

I want to interview you about the topic outlined above at a time and place that would suit you most and this would take between one hour to two hours.

What will happen to the information collected?

The information collected from the interviews will be used towards writing my PhD thesis and preparing presentations for national and international conferences and writing articles for publication at relevant journals. No participants will be named in any research output unless explicit consent has been given.

The recorded interviews will be destroyed once fully transcribed. Names of people, places, organisations or any information that would lead to identification of any of the interviewees will be deleted once the PhD is completed. The transcribed interviews will be kept secure, and only my supervisors and I will have access to them until I finish my PhD. The reason for material until I finish my doctoral research is in case I need to go back and check that the analysis has been done correctly.

Declaration to participants

If you take part in the study, you have the right to:

- Refuse to answer any particular question, and to withdraw from the study at any time.
- Ask any further questions about the study that occurs to you during your participation.
- Be given access to a summary of the findings from the study when it is concluded.



### IX.3 Appendix 3: Interview schedule

- ⊕ What is the definition of a “relationship with the client”?
- ⊕ How do relationships promote the transfer of information about the business in question from the small business to you?
- ⊕ What kinds of things increase your access to the firm’s private information?
- ⊕ What is the basis of a good relationship with a client?
- ⊕ How do relationships between you and the client develop (what steps do you go through to build it)?
- ⊕ What do you typically do/discuss when you meet clients for the first time?
- ⊕ What do you typically do/discuss when you have already a relationship in place?
- ⊕ How do you learn to make better banking decisions? What information is pertinent to learning about a firm’s credit eligibility?
- ⊕ Does the relationship between you (the loan officer) and the small business manager enhance the amount of information (about the small business, its manager/ employees/ suppliers/ customers) available to you and thus, help you make better decisions about lending to this small business and, therefore about the terms of the loan?
- ⊕ Even in the case of readily available information about the small business (from financial statements and other sources), does this kind of relationship help you to interpret this information correctly?
- ⊕ Does your relationship (as a loan officer) with the small business manager, his employees/ suppliers, and his general environment affect small business acquisition of credit and the interest rate charged over time? If yes, can you

please elaborate a little bit on this issue? How...

- ⊕ How can you decide if you have a strong/deep relationship with a client or if the relationship cannot be described that way? Can you measure this relationship using a Likert scale (1-7)?
- ⊕ Do you customize deals and create innovative risk-reducing financial instruments for your clients when they provide you with information and resources beyond that which they have made publicly available? If not, why not? Would you want to do so if you had the opportunity?
- ⊕ When the small business manager you usually deal with retires, dies, changes jobs...or is replaced by someone else, does your relationship with the firm changes? Do you need to start the relationship from scratch (the beginning) with the new manager or what? Please explain.
- ⊕ How many years have you been working in the banking industry?
- ⊕ How many years have you been in the industry? Have you worked at other banks and/or branches of this bank?
- ⊕ What kinds of industries do you lend to?
- ⊕ How many client firms do you have and what is the average number of employees at these firms?
- ⊕ Is relationship banking beneficial? Why and how is it beneficial? Then, what are the benefits of relationship banking (enumerate them)?
- ⊕ How do you go about securing those benefits?
- ⊕ Do you think relationship banking humanises the bank? How?
- ⊕ What are sources of information do you use to evaluate loan applications from SME clients? how and why? (hard data and soft data)

- ⊕ How do you process a loan application from a SME client? Is there specific steps you follow? What are the steps you follow? Who gets involved? How, and why?
- ⊕ Can you measure the strength of relationship with your customers? How? What criteria do you use to measure relationship strength?
- ⊕ What drives you and the bank to build/have relationship banking with small business clients?
- ⊕ About segregation of loan underwriting: knowing and measuring the input from each component (financials, collateral, character), is it possible? Is it done? How about at the bank level do you know whether it is done or no?
- ⊕ Do you use relationship banking as a marketing mechanism/tool and/or as an assessment mechanism/tool