ABSTRACT. This paper explores the processes of financial intermediation that are used by commercial banks in their interactions with SMEs in Poland. The paper develops an argument for examining the empirical realities of commercial bank involvement with the SME sector within the context of economic transformation by suggesting that the connection between them influences the trajectories of economic change within transition. The paper provides a history of re-organisation of the commercial banking sector in Poland, paying particular attention to the involvement of foreign capital and foreign banks as the trend towards increasing foreign participation is apparent in the Central European transition economies. The findings from this research suggest that there are some significant variations within the commercial banking sector in the approach to, and practices for, lending to the SME sector.

1. Introduction

Decision-making structures and processes used by commercial banks to deal with lending to small and medium-sized enterprises in transition economies offer an interesting angle on the study of economic transformation because of their ‘newness’ and their potential for indicating how finance from formal financial institutions has begun to interact with the SME sector in these economies. The development of structures and processes within commercial banks is striking in the context of a transformation economy because the banks are widely regarded as not having been decision-making organizations under the state socialist economic system (Berglof and Bolton, 2001; Kowalski and Janc, 1999; Van Brabant, 1997; Able and Bonin, 1994) and their development is regarded as a significant element of post-socialist economic transformation because of the changes associated with investment allocated by ‘market’ principles, rather than directed according to state plan. The development of decision-making structures (i.e. separation of evaluation from decision, centralization or decentralization of decision authority, the reliance on formal stipulations versus discretion) and processes (information gathering and verification, evaluation procedures involving project assessment and previous performance, collateral appraisals, monitoring capacities and inclinations for developing ‘relationship lending’, possible participation in shared schemes of collateral registration, and practices that facilitate the uptake and use of external finance by this sector of enterprises) in the allocation of financial resources to firms has significantly changed commercial bank practices of lending. This paper examines the developing structures and processes for decision-making for lending to SMEs by focusing on the practices and policies of commercial bank decisions in dealing with SMEs in Poland.

The perspective adopted in this research about the wider economic importance of commercial banks and their lending practices for small and medium sized enterprises is based on ideas about the potential for economic development and growth which are fostered through financial intermediation processes directing funds towards innovation activity (embodied at least partially in the SME sector) (Berglof and Bolton, 2001; King and Levine, 1993a; Shumpeter, 1934). The research in this paper draws on those ideas as both research backdrop and incentive, but attempts to use empirically based research to examine ‘actual’ commercial bank structures and processes of approach in a post-socialist context where commercial bank/SME interactions are relatively new. The
paper has three principal objectives: First, to initiate the practice of involving decision-making and process structures into the analysis of commercial bank lending, particularly in circumstances where activities surrounding lending are not long established; Second, to highlight some very tangible findings about commercial bank structures and processes in Poland that are relevant to discussions about the nature of finance available to and used by SMEs (some of which corroborate with findings of Johnson, McMillan and Woodruff, 1999 and Janc and Kowalski, 1999); And third, to develop theoretically and empirically grounded propositions for future research into process of financial intermediation that will further develop and expand the arguments and findings presented here.

The paper has five sections. The first section explores debates about SME financing and the role of financial intermediation for SME’s in transition economies; this discussion provides the wider context for research presented in this paper and considers the suitability of the employed methodology in light of the research perspective and objectives. The second section traces the recent history of banking sector development in Poland. The story told in this section illustrates how the post-socialist environment in which banks and SMEs are establishing relations and interacting is particular, suggesting that structures and processes for interacting and dealing with the emerging SME sector are developing within unique circumstances. The third section addresses the distinction between structure and process as means of influencing decision practices, examining how structure and process combine to overcome particular lending issues. The fourth section introduces the data from the interviews conducted with commercial banks in Warsaw, Poland. The presentation of data findings is interwoven with their discussion. This is the largest section and deals with themes revealed as important to how the banks deal with SMEs, namely: centralization/decentralization, hierarchy/dispersal, involvement of third party information as sources of evaluation information, and capitalization issues related to domestic/international ownership. The final section briefly reviews the findings presented in efforts to explore our understanding of how economic transformation is actually unfolding in the post-socialist sphere. This discussion allows for contemplations of theoretical and empirical propositions for further research in this area.

2. Debate and methodology

The development of decision-making structures and processes for commercial bank lending to firms in transition economies is a fundamental element of economic transformation that is not addressed in substantial form in the transition banking literature (As a notable exception see Koford and Tschoegl, 1997). The relative paucity of attention and research dedicated to the qualitative analysis of decision-making by commercial banks within transition economies relates in part to the focus on privatization, regulation, and corporate governance as factors and measurements of transition. Such emphases seem to assume that the financial sector, and in particular commercial banks, will develop adequate and appropriate procedures for dealing with risk in lending to firms if exposed to appropriate regulatory measures and may serve as a disincentive for examining industry norms and variations in how commercial banks structure and process decisions for lending. Expectations for ‘rational’ profit maximizing/risk-minimizing behavior by the commercial banks in transition economies, even when circumstances and realities of inherited bad loans and cyclical problems of government bail-out are recognized (Gray and Holle, 1996, 1997), may displace investigations of actual lending by suggesting that prevailing regulatory frameworks, conditions of uncertainty in the economy, risk associated with firm lending stemming from forms of informational asymmetries, dishonesty, and fraud are the principal factors influencing ‘rational’ bank lending behavior (For various discussions see: Bonin et al., 1998; Slay, 1996). The research in this paper actively acknowledges the vital role of larger scale commentary and analysis of financial systems in transition research and aims to contribute to this literature from a different perspective.

The research in this paper, which investigates the variations in approaches and procedural aspects of commercial bank actual engagement, recognizes recent empirical research into issues