Article

Socio-Economics and the Probability of Loan Approval

Marcelo Siles, Steven D. Hanson, Lindon J. Robison

Abstract

This study analyzes the influence of relationships on the probability of loan approval. Michigan banks located in communities with a population of less than 10,000 supplied the data for this study by responding to hypothetical loan requests. The survey results demonstrate that in addition to the usual financial performance variables, business and social relationships between lenders and prospective borrowers significantly affect the likelihood of loan approval. The effects of relationships on the loan approval decision are largest when information on the financial strength of the prospective borrower is mixed. In cases where the financial strength of the loan applicant is unambiguously strong (weak), the loan is likely to be approved (rejected) regardless of the applicant's relationship with the lender.

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