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SME Financing and the Deployment of Lending Technologies in Japan

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Abstract

The current literature on SME loan underwriting assumes that banks use just one of two lending technologies: relationship lending for opaque SMEs and transactions-based lending for relatively transparent SMEs. Recent work has departed from this view and hypothesizes that banks use a variety of distinctly different lending technologies. It emphasizes that the typical SME bank loan is underwritten primarily based on just one of these technologies and that many different transactions-based technologies are well-suited for opaque SMEs (e.g., Berger and Udell 2006). We test these propositions using data on Japanese SMEs and find that although financial statement lending is the most commonly used lending technology and serves as a kind of basic technology, it tends not to be used to the exclusion of other technologies. We also find evidence that the deployment of different lending technologies does not vary across different bank types. These findings imply that, at least in Japan, SME lending practice is generally inconsistent with much of the academic research on how banks underwrite loans.

Keywords: Lending technology, Financial statement lending, Fixed asset lending, Relationship lending, Small- and medium-sized enterprises

JEL Classification: G21, L14, D82, L22

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