State aid to banks and credit for SMEs: Is there need for conditionality?

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* The views expressed are those of the discussant and do not necessarily represent the official position of the EBA

Summary of the paper (2/2)

Goal: In cases where State Aid is provided to banks, assess whether setting conditions linked to SME lending can be justified legally and economically.

		Method	Sources	Conclusions
Legal justification	Are conditions legally allowed?	Review of EU State Aid rules	- Article 107 TFEU - Banking Communication from July 2013	Conditionality legally allowed
Economic justification	Are objectives linked to conditions on State Aid achieved?	Qualitative analysis: Case-by-case	State Aid Register of the DG Competition	Uncertainty on the impact as many programmes are not finished and no reporting on reaching individual objectives
	Does State Aid lead to increased SME lending?	Quantitative analysis at MS level: **DV-** Share of successful loan applications **IV of interest -** State Aid measures	-ECB SAFE Survey -ECB CBD -DG COMP State Aid Register	After the financial crisis SME lending fell more in countries with more State Aid for financial sector.
	Do specific conditions imposed to State Aid lead to increased SME lending?	Quantitative analysis at bank level: **DV-** net customer loan growth **IV of interest -** dummies for conditions	-CEPS-FIPP -DG COMP State Aid Register Also AMECO, EBF, NCBs	No evidence of SME finance conditionality leading to higher levels of SME lending

General remarks

Relevance

- Very important topic given the large amount of State Aid provided to banks during the crisis and a lack of understanding of how it actually is translated into effective lending to real economy.

Data availability

- Lack of data on SME - a common issue in the studies of SMEs. The paper has done most of the available data.

Assessment

- Confounding effects - Difficult to test due to other measures that are in place before State Aid.

Scope

- Economic justification: benefits are higher than costs. The paper focuses on the benefits of conditionality, but there is no further discussion of (potential) costs of these conditions.

Comments:
Quantitative analysis: Member state level

- Authors leveraged the SAFE survey for data on SME financing
- Dependent variable (**SUCCESS**) - SMEs successfully obtaining a bank loan

$$SUCCESS = \frac{obtained\ a\ loan\ in\ the\ past\ 6\ months}{demand\ for\ loans}$$

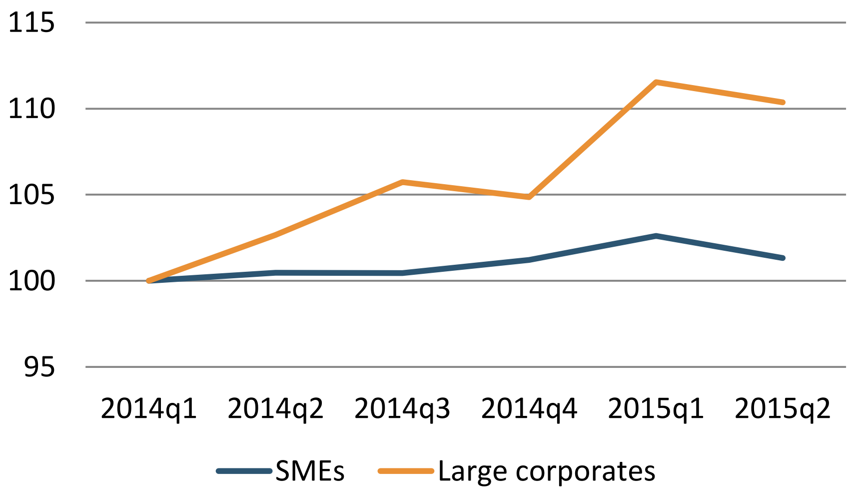
  - SMEs that successfully obtained a loan in the last 6 months – Received everything + Received 75% and above + Received below 75%. Did you consider separating the credit rationing effect – received less than 75%. (Casey and O'Toole, 2014; Ferrando et al., 2015)

- The negative relation between CAPITAL (equity ratio) and SUCCESS (share of successful application) is counterintuitive (as acknowledged by the authors) – however, in times of stress, when capital ratios prove inadequate and there is pressure on the banking sector to increase the capital this relationship may not necessarily hold (e.g. Aiyar et al., 2015, MAG, 2010)

Comments:
Quantitative analysis: Bank level

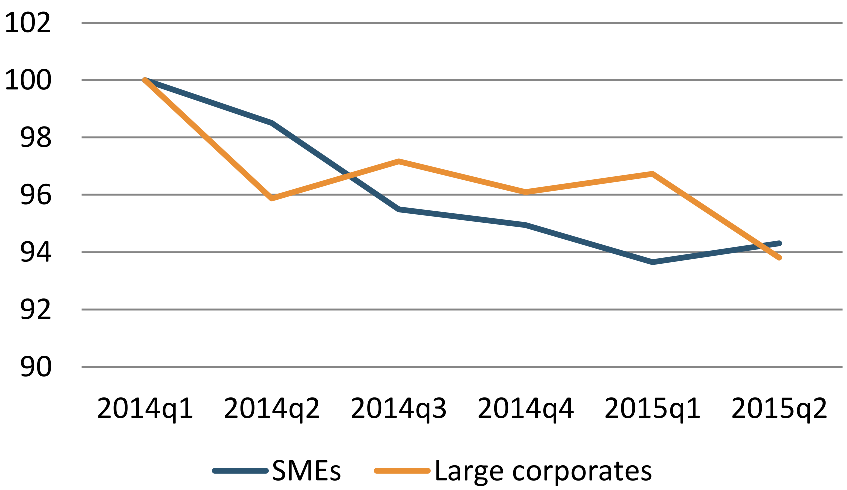
- The analysis is based on the paper of Brei et al (2015).
- Net customer loan growth (used as a DV) includes also corporations and households due to lack of data → Assumption that the composition of the loan portfolio (share of SME loans) does not change in the sample.

Capital Unconstrained Banks (2014q1=100) – SMEs vs Large exposures



Source: EBA Supervisory data

Capital Constrained Banks (2014q1=100) – SMEs vs Large exposures



Source: EBA Supervisory data

- State Aid and conditions may change the effect of other banks characteristic on lending

Ideas and extensions

Suggestions

- Try different definitions of the SUCCESS indicators, by removing the credit rationed SMEs from the successful applications
- Add lags or growth variables for capital in the assessment at member state level
- Use interaction of State Aid and conditionality dummies with bank characteristics in the assessment at bank level.

Extensions

- Analyse also the costs (or costs versus benefits) of conditionality – what benefit would be considered sufficient to justify the costs (e.g. see Aiyar et al, 2015)

Policy implications

SME Supporting Factor

- Capital discount hence can be considered as capital support for banks lending to SMEs
- No conditionality imposed
- BUT Recital 44 of the CRR says that the capital relief should be used to support SME lending → not legally binding
- Would it be more effective if conditions were imposed? Results suggest that NO.

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