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A Darker Side to Decentralized Banks: Market Power and Credit Rationing in SME Lending

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Abstract

We use loan-level data to study how the organizational structure of banks impacts small business lending. We find that decentralized banks-where branch managers have greater autonomy over lending decisions-give larger loans to small firms and those with "soft information." However, decentralized banks are also more responsive to their own competitive environment. They are more likely to expand credit when faced with competition but also cherry pick customers and restrict credit when they have market power. This "darker side" to decentralized banks in concentrated markets highlights that the level of local banking competition is key to determining which organizational structure provides better lending terms for small businesses.

Keywords: Geographic Location; Customers; Financing and Loans; Credit; Organizational Structure; Banks and Banking; Governance Compliance; Competitive Strategy;

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