FINANCIAL CRISIS AND LOCAL BANKS: A REVIEW OF BANK-FIRM RELATIONSHIPS IN ITALY

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Abstract

This paper focuses on bank-firm relationship in an economic deeply changing environment. The objectives of the paper are two-fold: to understand, compared to the overall banking system, if the lending activities and economic-financial performances of Italian local banks have changed after the outbreak of the financial crisis; and to understand what are the conditions that allow to develop a model of a local bank capable of supporting the development routes of SMEs, by an appropriate risk/return profile. In order to answer the first research question, the paper presented an empirical analysis, covering the period 2007-2011, of Italian Cooperative Credit Banks (a particular category of local banks) compared with the system of bank groups with operability spread over much of the Italian territory and not. The empirical comparative analysis has the aim to see the effects of the crisis on the relationship bank-firm through the reading of the impact on the dynamics of lending and on the profiles of structure, riskiness, profitability and efficiency of the banks under examination. In order to provide an answer to the second research question, the paper provides some insight of evolutionary nature reflection in the bank-firm relationship. In accordance with the doctrinal postulates of the relationship lending the empirical analysis shows how the financial then real crisis has not induced Cooperative Credit Banks to restrict credit to local firms. The survey evidences have however highlighted some critical elements that are reflected inevitably on the local bank's risk-return profile. Based only on quantitative data of statement, the empirical analysis represents a limit in this kind of research. This paper is useful to stimulate the debate of experts as well as to focus on the studies of local banks in particular in the light of their anti-cyclic role. Even if abounding in subjects about local banks and relationship lending literature faces only marginally the effects of global crisis on business profiles of local banks.

Keywords: Local Bank, Relationship Lending, Credit Risk, Global Crisis

1. INTRODUCTION

Local vocation banks or, simply, "local banks", "territory banks" or "relationship banks", "community banks", "development banks", or "district banks" (Baccarani, Golinelli, Rullani, 2013; Bonfanti, 2009), have been, in the recent past, subject, as major or national banks, to great changes due to the pressure of market and regulation factors on the one hand, while on the other hand, to the effects and implications of financial crisis started in August 2007 and the recession of real economy that followed.

However, the developing transformation has confirmed how local banks have reduced at level system, overweight financial activities compared with lending activities (Minnetti, 2011, 2013); local banks, usually small banks, as for example, cooperative banks (BCCs), have shown a certain vitality to defend and, in some cases, to increase their competitive market positioning in the observance of the essential reasons of their mission. This contribution of research intends to examine the role of local banks in the present, competitive scenario particularly to their connection with the enterprises.

More precisely, we want to verify if during the years of crisis these institutions have continued to represent the primary interlocutors of SMEs, their traditional reference clientele in consideration of commitments, supporting in any case, financial requirements and credit rationing in a lower measure in comparison with what registered at "system level".

Based on this study, the major hypothesis is about to understand whether and how by exploiting the traditional strengths of the rooting on the territory and the ability to develop and privilege relation connections with their own customers in the relationship banking approach, local banks have assisted the productive sector and have been able to face the hard, economic situation which started with the summer recession of 2007 with a relevant Italian slowdown of bank loans and a strong deterioration in the quality of assets and liabilities.

Even generally considered, this phenomenon has taken different features according to the size of the bank. During the years between the most acute phase of crises, loans issued by major banks have registered growth rates clearly below what discovered with reference to smaller banks. On the contrary, the deterioration of exposures has interested mostly small, minor banks. Further, the study intends to understand whether and how the economic and financial profiles (structure, profitability, efficiency and risk) of local banks (BCCs) have changed as regards the effects of financial and economic crisis. The Cooperative credit is a system based on a network comprising 404 cooperative banks called Banche di Credito Cooperativo (BCCs).

In particular, the study is carried out by the formulation of two research questions: R.Q.1) What are the effects of financial crisis on lending activities and economic-financial performances of Italian BCCs in the period 2007-2011 compared with the total banking system? R.Q.2) What are the conditions that allow to develop a model of a local bank capable of supporting the growth, development routes of SMEs, by an appropriate risk/return profile?

On the base of research questions there is an approach to the research structure that develops methodologically as follows.

The second paragraph offers a review of the main theoretical contributions about the local banks and the relationship banking as a relational approach with customers. The topic of the relation between a local bank and related system with clientele arises as a premise in the discussion aimed to capture the reflections on credit dynamics to SMEs.

In order to answer the first research (R.Q.1), the third and fourth paragraphs present an empirical analysis, covering the period 2007-2011, of Italian BCCs compared with the system of bank groups with operability spread over much of the Italian territory and not.

The empirical comparative analysis has the aim to see the effects of the crisis on the relationship bank/firm through the reading of the impact on the dynamics of lending (core business of local banks) and on the profiles of structure, riskiness, profitability and efficiency of the banks under examination.

In particular, the third paragraph offers an analysis of the dynamics of credit of the sampled banks; borrowing, in the method, Minnetti's scientific contribution (2013), the analysis of the dynamics of "lending" activity is carried out examining the trend in the 2007/2011 period of three balance sheet/income statement items to be significant for the representation of the relationship between a local bank and a company: Credits with customers; Non performing loans; Credit write-down (Value adjustments on credit).

The empirical analysis continues in the fourth paragraph with the looks of the different profiles of the BCCs through a system of ratios so distributed for each profile: structure (Net assets ÷ Total assets, Total collection ÷ Total assets, Due from customers ÷ Direct deposits); riskiness (Value adjustments on credit ÷ Credits with customers); profitability (Net interest income ÷ Net interest and other banking and insurance income, Profit/loss for the year ÷ Net assets); efficiency (Cost income ratio: Operating expenses ÷ Net interest and other banking and insurance income).

As we anticipated and in line with the objectives of the paper, surveyed banks are sampled in two categories respectively denominated, banking groups (dimensionally large banks, with widespread operation at national level and by nature with little local vocation) and BCCs (local small banks and highly suited to the operational area).

With the reference to the first once, the analysis examines the last five financial statements (period 2007/2011) of a sample of 14 banks organized as limited companies (Spa) and having widespread operation throughout the national territory, while the sample of BCCs consists of all the institutes operating in Italy (404) in the form of cooperative bank.

The overall sample has a good statistical significance since it covers the 59% of the universe of active banks at the end of 2011.

The financial statement are processed not as absolute values, but as rates of change in comparison with 2007 (taken as the base year).

In order to provide an answer to the second research question (R.Q.2), the fifth section provides some insights of evolutionary nature reflection in the bank-enterprise relationship.

In particular, useful considerations were formulated about the need for the local bank to enrich the operational and related contents of the relationship with companies, each with its own complexity, through the development of services to the support and sometimes to the accompaniment of SMEs live path in the respect of the role of the local bank and environment in which the bank and enterprise operate.

2. LOCAL BANK AND RELATIONSHIP LENDING: A LITERATURE REVIEW

This section of the paper provides an overview of the main national and international studies about the role and characteristics of local banks and relationship lending as a relational approach to customers.

There has been developed an intensive debate on the role and characteristics of the local bank that was still going on, appeared in the late 90's when they started off the merger transactions among banks in the Italian banking system. With the term "local" they identify a very wide universe of banks that covers this case in point also very different among them.

According to Alessandrini (1994), the local bank stands out from the national bank as characterized by a strong interdependence with the social and economic community (regional or sub-regional area) in which it operates.

Also Ferri (1995) and Pagano (2000) share this approach by defining “banking localism” a phenomenon associated to the small sizes and credit institutions with registered office and much of the distribution network in a certain administrative context (Province or Region).

Comana (2006) focuses on regional banks, that he defines as those intermediaries which carry out their activities in a territorial area, though not delimited geographically within the borders of a region.

The study of Bonaccorsi Di Patti, Eramo, Gobbi (2005) introduced a quantitative parameter: the local bank would have an active less then 7 billion euros, including in this process both small banks (assets between 1 and 7 billion euros) and the minor banks (assets of less then 1 billion euros).

According to Bongini, Di Battista, Zavarrone (2007), a bank is defined of small size if three features at least prevail: the long-term relationship, the peer monitoring and functional proximity between business centres of the bank and the operating offices of the enterprise to be financed.

In another contribution, Alessandrini, Presbitero, Zazzaro (2008) focused on the role of “disctrict bank”, stressing that the specific nature of the enterprise-bank connection within these areas depends on both the characteristics of local firm and the type of the local credit market described by the reference territory and that it is easier than in the district areas an exclusive and recent relationships are consolidated.

From the point of view of the competitive model, we know what the advantages of local banks are (Farabullini and Gobbi, 2000; Guiso, Sapienza, Zingales, 2004): the operating cultural geographical proximity with the company, the managing of customers’ relationship; the acquisition of information on the territory and clientele, which translates into an informative advantage in the evaluation of loans; the short and fluent organizational structure, that determines the ability to get information and rapidity in responding and decision making.

All those results in a strong commercial penetration in the retail market and in a direct and privileged knowledge of the enterprises granted, through a customer monitoring facilitated by the localism itself and the possibility of social control that goes beyond a formal contrast.

Some elements of criticality are opposed in an equally clear manner and verified: in acquiring the skills and resources for the construction of more sophisticated management models to be employed in the finance and credit area; in the diseconomies of scale in their use; in the articulation of a diversified loan portfolio that optimizes the risk degree; in the expansion of the range of products/services to offer to business customers.

In the summary evaluation that is usually proposed, through an approach to its customers typically relactional, the local bank is better placed to know and assess the needs of their territorial companies and to channel the savings on it, making this way the funding circuite more direct and reducing phenomena and costs of multiple intermediation.

As regard the theme of relationship lending, literature fails to provide a single definition. Starting from the 90’s different authors provide definitions complementary among them.

The contribution of Ongena and Smith (2000), analyzes the theme in terms of: «Relationship that goes beyond the execution of simple and anonymous financial transaction». Also Boot (2000) provides a definition of relationship banking, expressed as following: «The provision of financial services by financial intermediary who: i) carries out expensive investments to acquire confidential information about each customer funded, which, often, become the exclusive property of the middleman broker; ii) estimates the profitability of the “informative” investments done and the opportunity to repeat them later». To define the concept of “relationship lending” there is a need to refer to Elsas’ (2005) contribution: «An implicit long term contract between a bank and its debtor».

The aforesaid research contributions show how in the relationship lending the granting of credit is determined by a number of so called conditioning factors:

- Clientele relationship that units the trusted one to the bank by the existing loan contracts and/or deposit.
- The assumption of “direct” and “confidential” information, beyond the available. The same information can be renewed and enriched during the course, overtime of the relationship, non only of lending, but increasingly extended to other services offered by the bank.
- The wealth of information accumulated remains the exclusive domain of the bank.

Recently the attention of researchers has focused on the ability of financial intermediaries to gather soft information (qualitative information usually reserved). Berger and Udell (2002, 2006) define, more precisely, the long-term banking relationship as a credit assignment technology that depends on the production of soft information.

The relationship banking goes beyond the loan and can include additional financial services as well as feasible by investment banks and non banking financial brokerage.

Boot (2000) argues that the most appropriate term would be “relationship intermediation”; however our focus is on relationship lending. This concept emphasizes that the bank is the one that makes the investment necessary to obtain specific information from the borrower; as result, the customer can accept or not to establish a relationship with the bank (Freixas, 2005).

Banks can use a variety of technologies for their loan business, that includes the technologies of transaction and different loan relations (Boot and Thakor 2000; Berger and Udell 2002).

Relationship lending sees the bank to adopt behavioural patterns, in the relations with trend business customers, tending to close monitoring, to renegotiation of mortgages, to implicit long-term contractual agreements and to the collection of “soft” (reserved) information over time.

On the contrary transaction lending privileges quantitative, standardized information and a relationship with a user oriented individual transaction (transaction) – in relation to that it measures the profitability of the customer – rather than the ratio as all.

The transactional bank does not bother to collect confidential information (soft information) but it focuses on the development of objective indicators of qualities (financial ratio) by which to evaluate their own client in respect of each product delivered.

As the information used (hard information) is available also to other intermediaries, financial credit institution assumes no privileged position and then, in the face of considerable saving of costs for the collection of information, it does not benefit of the monopolist income generated by the knowledge of the actual risk profile of the customer.

Overall, in transaction lending the loan is subject to the collection of transparent high quality information; from this favouring borrowers able to report, credibly, their solvency.

Relationship lending is indicated especially in dealing with customers characterized by the physiologically "opaque" information structure, (for example young companies with little tradition in the relationship with the banking system and/or without guarantees).

Jayaratne, Wolken (1999) and Berger, Udell (2002) shoe how small banks hold significant competitive advantages in relation to the management of reserved information. In effects, recent research contributions emphasize the role of small banks in the soft information collection and the importance of their organizational structure to be used (Stein, 2002; Takats, 2004; Berger and Udell, 2002; Berger, Miller, Petersen, Rajan, Stein, 2005); in particular, many recent studies have focused on organizational and operative variables of banks and on the link between these ones to the effective use of the information in the process of assignment.

These studies intersected with the studies on the proximity between the customer and the bank and focus on the internal organization of the latter, starting from the assumption that organizational forms characterized by multiple decision levels – typically pyramidal organizational structure – compared with flat organizations, they seem less suited to use effectively non encoded and non standardized information, so called soft (Stein, 2002).

For this hypothesis, empirical support was provided by the study by Berger, Miller, Petersen, Rajan, Stein (2005), which shows how, compared to small banks, larger intermediary banks tend to provide loans to customers located further away, to larger companies and to make a greater use of coded information (so called "hard").

Literature on relationship lending has identified many benefits and some costs of these relations; first of all, Boot (2000) who gives a very detailed explanation on the cost-benefit relationship lending and related implications. Later, integrating them with some recent contributions, Boot's (2000) key insights will be summed up.

The adoption of relationship lending in bank-company relation has several important advantages. In fact, the exchange of confidential information between banks and enterprises enable enterprises to have a great amounts of credit, to create value for shareholders and improve company performance.

Relationship lending makes easier, in particular, the exchange of information between the debtor and the payer. Debtors prove to be more inclined to reveal information to banks due to the increased confidence of relationship (Yosha, 1995): «The relationship bank-enterprise takes on connotations strictly confidential. The information revealed to the bank are not disclosed to other lenders or to competition and, in the same time, they allow the company to obtain the credit needed to finance its investment projects, without having to reveal publicly the same information. Their acquisition allows, in the same time, to the bank to perform its monitoring activities. So, confidentiality produces positive effects for the company as it reduces the risk of credit rationing. This aspect becomes especially important when funds are used for R&D projects».

The low information asymmetries favoured by relationship lending allow to go beyond problems of moral hazard and adverse selection inherent to credit markets. In particular, the idea is that the longer the relationship between banks and business is, the closer is the informational link between the parties and more reliable appears to the bank the owner-entrepreneur; this avoiding the risk of moral hazard (Diamond, 1984, 1991) and reducing agency costs triggered by the management behaviour (Weinstein and Yafeh, 1998; Jensen and Meckling, 1976; Chiesa, Palmucci, Pirocchi, 2009).

Relationship lending allows, beside other benefits, a greater flexibility in renegotiating contract terms and some discretion in modifying technical form of loan (Boot, 2000).

Thanks to the soft information owned assets and to the medium-long term targets, the bank can therefore guarantee the company more flexible conditions. However, customer relations induce the debtor to behave more virtuously for two reasons: the former is due to the continuous monitoring of the bank; the latter resides in warranty, or implied promise, that the bank will offer new loan disbursement in the future to better conditions (in terms of cost, amounts and guarantees).

In short, the stability of relationship favours not only the ex ante determinations of contract conditions but also the ones of any future loans (Rajan, 1992).

3. IMPACT OF ECONOMIC DOWNTURN ON THE BANKS' LOAN

In the light of the content and evolution of the literature on banking localism and relationship lending, we have proceeded to carry out an empirical verification aimed to examine the dynamics of the loans granted by local banks during the crisis years in order to understand how their core business (credit intermediation services) was impacted by the economic financial environment of recent years.

Empirical research has allowed us to verify if the international crisis has produced significant impacts on the management mode of relationships with customers by BCCs, defined as "territory banks", favouring therefore, a change in their operational identity from an intermediary more focused on traditional intermediary lending, to an intermediary with a more significant ability to diversify his offer model in the sector of movable brokerage.

Coherently with the objectives of the paper, the surveyed banks are sampled into two categories named, national banks and BCCs respectively.

Referring to the former, the analysis examines the last five financial statement (2007/2011 period) of a sample of 14 banks (that is 14 banking groups considered among the larger ones dimensionally based on the classification made by ABI) with widespread operation throughout the national territory (Table 1), while the sample of BCCs consists of all institutions operating in Italy (404) in the form of cooperative bank.

Table 1. The banking groups investigated

Intesa Sanpaolo
Unicredit
MPS
UBI
Banco Popolare
Banca popolare dell'Emilia Romagna
Banca Popolare di Milano
Banca Popolare di Sondrio
Banca Sella
Banca Marche
Banca popolare di Vicenza
Carige
CREDEM
Credito Valtellinese

In relation to BCCs, the check was performed through the use of Federcasse data base while the financial statement data of 14 banking groups were obtained through access to their corporate websites.

The total sample has a good statistical significance since it covers 59% of the universe of active banks at the end of 2011. Financial statement data are processed not as absolute values, but as rates of change compared with 2007 (Taken as the base year). With reference to the performance of the first magnitude of the balance sheet analyzed, that is the "Credits with customers", there are some differences between BCCs and bank groups (Table 2).

Table 2. Credit with customers

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Credits with customers	10,41%	9,45%	11,16%	11,13%
Local Banks (BCCs)				
Credits with customers	12,21%	21,82%	31,46%	34.98

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

During the reporting period (2007-2011) "due from customers" reveal increasing for both categories of banks investigated.

However, the BCCs register higher percentage changes of growth; besides to record a rate annual average growth of loans to customers that is 25,12%, more than double compared with that for banking groups (10,53%), they are characterized by the systematic and increasing trend of annual growth rates. Banking groups, instead, are characterized for the dynamics in lending more fluctuating (and less intense).

On the whole, therefore, local banks maintain in the period examined, their competitive position, showing a good dynamic characteristic.

This first empirical evidence underlines the presence of a direct relationship between the size of the bank and the dynamic of credit extended to customers and a strong preference for local banks to adopt business models focused on traditional lending (marked by the centrality of loans to customers) following the management approach of relationship lending and less on movable brokerage[11].

To this regard, it is also useful to analyze the weight of such activities within the operations of the bank by calculating the ratio Credits with customers ÷ Total assets.

The good dynamics of loans to customers have seen BCCs register a minor reduction of the parameter. The datum, as a whole, confirms what is already clear and the fact that local vocation banks are more structured on lending activity, that remains central in the corporate policy and that continues to be their own mark (Table 3).

Table 3. Credits with customers ÷ Total assets

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Credits with customers (% Total assets)	-3,91%	-1,81%	-2,38%	-4,01%
Local Banks (BCCs)				
Credits with customers (% Total assets)	0,72%	-0,26%	0,50%	0,50%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

Strictly complementary to the analysis of the dynamics of loans there is the examination of impaired exposures, represented prevalently from "non performing loans" (Table 4) and "credit write-down" (Table 5).

Table 4. Non performing loans

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Non performing loans	25,49%	46,83%	107,68%	154,24%
Local Banks (BCCs)				
Non performing loans	31,89%	93,16%	159,71%	235,84%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

The trend of non performing loans from 2007 to 2011 indicates for banking groups a constant percentage increase, with the data that grows systematically in the period under observation. The dynamic of BCCs is worse so that it marks in the 2007-2011 period an average rate of change of 235, 84%. These evidences underline how the lending process has been, generally, characterized by the significant deterioration in credit quality during the years of international crisis. BCCs report the highest percentage values, above all starting from 2009 when the crisis influenced also the real economy; these evidences are consistent with the results of the empirical research by Tutino, Colasimone, Brugnoni (2012) and Minnetti (2013).

Tutino's analysis on the credit granted by Italian Banks, distinct by size, over the years of international crisis, shows that there is an inverse relationship between growth impaired loans and bank size.

As Tutino says: «The reasons of heterogeneity found in the trend of credit to clientele according to bank size, can and must be traced in the different specificities found in the brokerage model adopted by banks and in different arising vulnerabilities. In other words, there is a significant relationship between specific features of the brokerage model adopted, underlying management strategies and performance of the credit to customers. The smaller size Banks, characterized by a business model more

[11] Similar conclusions were reached by Tutino, Colasimone and Brugnoni (2012).

oriented to traditional lending business with customers than the larger ones and characterized by less vulnerable strategies and political management intermediation strategies, are the ones that during the recent financial crisis, have argued, more vigorously, the real economy by providing credit to customers».

The findings from Tutino's analysis, therefore, provide useful information to explain and, somehow, justify the greater non performing loans that characterized the operation of BCCs compared to bank groups.

The increased deterioration of the quality of the credit issued has been the cost that small banks, traditionally oriented to lending business, have had to incur, in order not to loose their competitive position and their identity of local bank.

In this respect, we would like to stress as to the different dynamic, in front of bank groups, of non performing loans, must match a grip of awareness of local banks of the need to pursue, preserving the identity of local banks, an increased financial diversification of their offer model (Arnone, Bechi, Modina, 2013; Arnone, Modina, Quintiliani, 2013).

Empirical evidences on non-performing loans by the bank are also confirmed in relation to the performance of "value adjustments on credits" (Table 5). Starting from the business year of 2010, the analysis shows how banking groups record a decline in the parameter, differently from BCCs that, instead, see the value grow systematically in the period under observation.

Table 5. Credit write-down

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Credit write-down	136,52%	345,26%	259,68%	240,58%
Local Banks (BCCs)				
Credit write-down	61,08%	100,14%	123,88%	192,46%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

In synthesis the data extracted from the sample of selected banks show how local banks, in the period under review, recorded a growth in lending to customers, core business and the main item of balance sheet, that grew in whole more than what has been experienced for more dimensionally large banks and with widespread operations nationwide.

On the contrary local banks have reported growth rates of non performing loans and credit write-down higher than other banks.

Consistently with the results of Minetti's analysis (2013), also our investigations, therefore, allow us to say that in the years of the crisis, local banks have continued to support the entrepreneurial fabric, while remaining faithful both to their role as privileged partners of businesses and families in the territory and a business model based on credit intermediation.

This allowed them to ration credit to firms to a lesser extent than larger banks, even if, not being able to limit the negative effects of adverse economy with a dynamics of performing loans and credit write-down showing a problematic trend.

4. THE EFFECTS OF THE CRISIS ON THE PERFORMANCE OF BCCS AND BANKING GROUPS

Complementary to the analysis developed in the previous paragraph, here we try to grasp how financial crisis has impacted the profiles of structure, riskness, profitability and efficiency of banks under observation. The analysis of different profiles of sampled banks is conducted by a set of ratios.

As regard the analysis of the structure profile, the first ratio "Net assets ÷ Total assets" provides a measure of the capitalization level of banks. Observing the trend of ratio (Table 6) is evident how the earliest years of international crisis, small banks and banking groups have seen the impact of their net assets on total assets both suffer a gradual fall; however BCCs compared with national banks recorded the steady and systematic reduction of the ratio.

Table 6. Dynamics of structure index: Net assets ÷ Total assets

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Net assets ÷ Total assets	-5,96%	0,11%	-8,02%	-15,89%
Local Banks (BCCs)				
Net assets ÷ Total assets	-4,08%	-5,62%	-5,01%	-16,52%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

Remaining in the analysis of the profile structure, the second ratio, under observation, "Total collection ÷ Total assets" expresses the incidence of debts with customers and debts represented by bonds, savings deposits, certificates of deposit, spot against forwards on total assets.

This ratio provides a measure of heavy level debt supported by banks. Small banks, compared with bank groups, record a stable growth of the parameter that is more intense until 2009 (Table 7).

The recession and the aggravation of the crisis of sovereign debts has made more difficult and costly the placement of bond issues, while the increased competition in funding close to customer led to an increase in the interest rates on deposits.

The combined effect of these two factors, as it emerges from the dynamics of parameter, has influenced on the composition of the debts of banking groups, by imposing them the research of forms alternative to traditional funding; vice versa, local banks, pegged to traditional models of corporate lending, are characterized by the lack of poor financial flexibility and low propensity to develop more complex fundraising activities of those ones either to pursued.

Table 7. Dynamics of structure index: Total collection ÷ Total assets

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Total collection ÷ Total assets	-0,03%	0,11%	-5,55%	-7,48%
Local Banks (BCCs)				
Total collection ÷ Total assets	4,07%	6,71%	3,80%	0,29%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

Continuing to examine the structure profile, the third ratio "Due from customers ÷ Direct deposits" expresses the intermediation ratio referred only to the operation exchanged with customers. This ratio provides a measure of the propensity of banks to carry out lending operations, "stricto sensu", and therefore it can help us to express some consideration about the strength of relationships that these banks have established with customers. This because, as by prior empirical evidences, the lending and the funding represent the core business of the macro category of local banks of which BCC s are a particular expression.

The ratio dynamic (Table 8) confirms what has been shown in literature about the distinctive characters of the operations of local banks. Respect to banking groups, BCCs show substantial and stable decline of the indicator; this decline is justified by the progressive increase in direct deposits as a channel privileged by small banks to obtain financial resources.

For their part, after a decline in the years immediately following the arising of international crisis, banking groups register the stable growth of the index; this last empirical fact highlights the lower incidence of funding in operational choices of banking groups and support the hypothesis formulated in literature that sees dimensionally bigger banks moving towards the business models of corporate banking.

Table 8. Dynamics of structure index: Due from customers ÷ Direct deposits

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Due from customers ÷ Direct deposits	-3,06%	0,07%	3,13%	2,90%
Local Banks (BCCs)				
Due from customers ÷ Direct deposits	-3,22%	-6,53%	-3,18%	-0,29%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

With reference to the analysis of the risk profile, the indicator used to catch the dynamics of credit risk in the credit cooperative system is delivered in terms of "Value adjustments on credit ÷ Credits with customers".

As a result of global crisis, the values of this indicator have decreased significantly for banking groups, but increased, without knowing set backs for small cooperative banks (Table 9).

This different dynamic confirms what emerged before analyzing the trend of non performing loans during the period considered.

Despite a less favourable economic and financial environment, BCCs have implemented an indiscriminate and intense policies of allocation of credit by agreeing to bear the cost of higher deterioration in the quality of loans[12].

These findings allow us to affirm that small banks, with operations traditionally anchored to lending activities, must necessarily revise their scoring models, in order to ensure better integration between hard and soft information (Del Prete, Pagnini, Rossi, Vacca, 2013).

The question of the information advantage of him who is physically closer to the territory, than bank groups with notoriously centralized structures that rely on objective information (hard information) or "per tabulas", requires to be better rationalized, coming out of a too simplicistic representation.

It's really true that hard and soft information requires a more balanced mix (having passed in the credit approval practices by the excesses of the mere personal knowledge of customers to those of impersonal knowledge) but the rhetoric of "looking at the entrepreneur's eyes" must be disproved as a means to establish its reliability as a credit counterpart.

His history is important, but is not sufficient to assess the quality of the projects that he has in mind to realize and it cannot be a diriment element when no positive factors emerge from official documentation.

Table 9. Dynamic riskiness index: Value adjustments on credit ÷ Credits with customers

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Value adjustments on credit ÷ Credits with customers	-244,08%	-323,69%	-270,67%	-299,33%
Local Banks (BCCs)				
Value adjustments on credit ÷ Credits with customers	43,55%	64,29%	70,30%	116,67%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

With reference to the analysis of the profitability profile, the first ratio being surveyed is "Net interest income ÷ Net interest and other banking and insurance income". This ratio provides information on the scale of bank deleveraging. Lower values of this ratio denotes the increased ability of the bank to generate income outside traditional lending activities. In comparison with 2007, average rates highlight some differences between the two categories of banks placed under observation, particularly interesting (Table 10).

Table 10. Dynamic profitability index: Net interest income ÷ Net interest and other banking and insurance income

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Net interest income ÷ Net interest and other banking and insurance income	19,92%	1,58%	-1,37%	-0,28%
Local Banks (BCCs)				
Net interest income ÷ Net interest and other banking and insurance income	1,89%	-11,41%	-10,21%	-8,09%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

[12] A similar phenomenon was detected by Baravelli, Feliciotto, Mazzù (2002) for BCCs operating in Sicily, Italy

With reference to banking groups the ratio shows an increase until 2009 and then a decrease, but with low intensity in the following years. Change rates, rather marginal, indicate how banking groups, despite the difficult economic climate, have managed to achieve in the contest of production processes of income flows, a balanced mix between money management and management of the services.

The systematic, variable rates, of negative sign recorded by small BCCs can be interpreted as inclination of local banks to extend, in the logic of relationship banking, the range of products/services offered with a mix of high-value-added services and having consultancy and innovative content; from this, more able to assist the customer's business at a time when they face extraordinary transactions (such as services relating to placement and trading on behalf of customers).

The dynamics of ratio leads us to develop some reflections on the condition that can encourage or discourage the expansion strategies of the areas of operations (business areas) of local banks.

As Minnetti says (2013): «If financial activity favoured by the direct knowledge and continuity of relationship over time, is and will continue to represent the core business of local banks, there is the need for them to create an effective intervention space in offering innovative and complex services that is visible and recognized by the market».

Minnetti's considerations lead us to highlight plausible operating limits of local banks that prevent or slow down the implementation of strategies of diversification or deleveraging: availability of personnel with appropriate skills; availability of products/services to offer in addition to the traditional ones.

Such limits will necessarily require operational solutions, such as personal side, investment in training and search for adequate expertise to diversify business areas.

Side products/services, operational solutions specifically adoptable could lean towards a rethinking of organizational assets in favour of organizational assets of network type with aim of seeking economies of scale and economies of skills and reaching sizes that can ensure economic survival.

With reference to the advantages of banking network, it is interesting the research work by Modina and Polese (2008) offering a particular configuration of networks applied to local banks namely polycentric network.

In this particular reticular organizational structure each local bank acts as an equal partner in activities such as the designation of the government, the evolution of participation process and the release of resources.

In this system, all nodes, that is individual local banks, have the same size and maintain a reciprocal relationship with all relevant territorial and socio-economic actors.

In this framework, local banks could keep their competitive advantage compared to the larger ones, strengthen their economic situation and become a vehicle for innovation.

Continuing our analysis on the profitability profile, the second and final ratio under observation "Profit/loss for the year ÷ Net assets" measures the return on equity of the bank.

The crisis has caused a decline of this indicator either for BCCs and banking groups (Table 11).

Table 11. Dynamics of profitability index: Profit/loss for the year ÷ Net assets

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Profit/loss for the year ÷ Net assets	-24,19%	-24,22%	-24,27%	-24,92%
Local Banks (BCCs)				
Profit/loss for the year ÷ Net assets	-4,88%	-16,59%	-32,81%	-16,27%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

Excluding 2010, banking groups register a parameter contraction much more intense than BCCs. For small cooperative banks the contraction of return on equity begins to assume an alarming rate starting from 2009. In particular in 2010 the decrease is more than 30 percentage points; in 2011, the decrease was less pronounced. These empirical evidences show how the unfavourable economic situation, outlined as a result of crisis, is worrying for all types of banks surveyed. Whatever is the solution to adopt, there is no doubt that the shrinking of net interest income (lower profitability of lending activities) must be offset with the desirable increase in net interest and other banking and insurance income and in other net banking income. With reference to the analysis of the "profile of efficiency", the ratio considered is the cost-income ratio that is "Operating expenses ÷ Net interest and other banking and insurance income". Its reduction means that the incidence of costs, compared with the wealth produced, decreased so that the bank is more efficient.

In the years immediately following the outbreak of international crisis (and thus at the stage when it took the characteristics of a purely financial crisis, later real) banking groups show a lower efficiency; in effect, annual growth rates up to 2008, register greater percentage values with respect to BCCs (Table 12).

Table 12. Dynamics of efficiency index: Operating expenses ÷ Net interest and other banking and insurance income

	Average rate of change			
	2007-2008	***2007-2009***	***2007-2010***	***2007-2011***
Banking Groups				
Operating expenses ÷ Net interest and other banking and insurance income	10,88%	-11,00%	-2,95%	-2,94%
Local Banks (BCCs)				
Operating expenses ÷ Net interest and other banking and insurance income	8,36%	18,77%	26,25%	20,73%

Source: Our elaboration on Federcasse data (BCCs) and Financial statement data (Banking groups)

Starting from 2009, when the financial crisis becomes real, banking groups see the shrinking of the incidence of their operating expenses, while BCCs recorded a progressive growth of the parameter.

The growth trend confirms the difficulty of BCCS to ensure optimal coverage of operating expenses thanks to income flows coming from trading and hedging activities (Net interest and other banking and insurance income and other net banking income); also, this empirical evidence shows how the business model of local banks, as primarily focused on traditional corporate lending and less oriented to corporate banking, underweight the offer of services with higher added value.

5. CONCLUSION

The analysis of annual financial statements proposed here, in line with the emerging evidences from the literature review, has confirmed that the banks at local vocation, in the crisis years, have largely retained, if not slightly increased, their competitive position in the credit market.

The survey evidences have however highlighted some critical elements that contrast with the advantages highlighted in the review (see the second paragraph) and that are reflected inevitably on the local bank risk-return profile; such criticalities belong, in general, to the following:

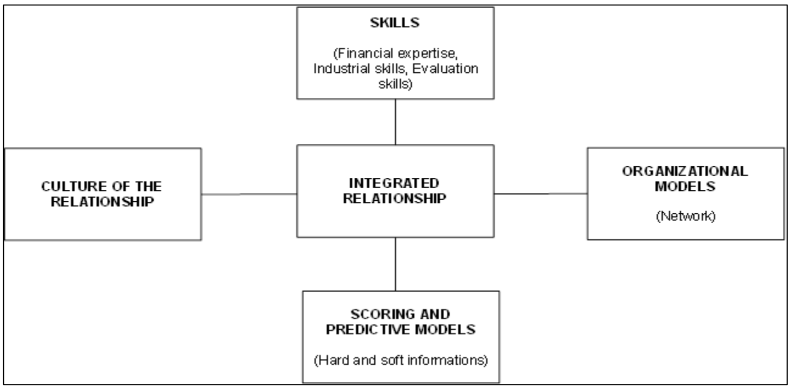
- Problematic trend of non performing loans (progressive deterioration of loan portfolio);
- Little diversified portfolio of loans and unable to optimize the risk profile;
- Low financial flexibility and low propensity to develop collection strategies more complex than those pursued;
- Scarcely adequate rating models in terms of combination hard-soft information;
- Poor range of products/services to offer to customers in addition to the traditional ones;
- Scarcity of skills and resources to develop policies for the diversification of business areas.

The proposals for improvements that emerge from this work are:

- The expansion in the range of services;
- Innovation in evaluation of creditworthiness assessment;
- Investment in training and appropriate professional recruitment to diversify business areas;
- Development of new organizational models (network building).

If small banks do not want to be crushed by the growing competitive dynamics which favour the largest banks, they will necessarily have to implement strategies to achieve a greater diversification of their business activities, considering the management culture of the relationship (namely the relationship lending approach) a strategic lever on which to focus in the redefinition of their vision and mission, to increase/to maintain their profit margins and offer that support of services and finance which identify the business of corporate banking. The following figure (Fig. 1) identifies desirable areas of strategic intervention that allow, effectively and above all rapid, the shift from business models focused primarily on traditional lending activities to business models that can promote closer integration between corporate lending and corporate banking.

Figure 1. An integrated model of relationship (or the model of corporate banking relationship)



After all these considerations above exposed I wish point out that, in a context of crisis, local banks must necessarily play a role in different fields but closely related to the logic of continuing to be a solid reference point and capable for the companies they continuously operate.

As Minnetti stated (2013): «If, in fact, the lending has always been the fundamental reason for the existence of local banks, it is clear that it can be no longer the only funding for firms, especially for the dynamics ones and with potential development. Equity resources, share and bond issues on markets, structured financing operations are some of alternative funding formulas that firms could require to which the financial intermediary system, in its different components, must respond with the preparation of a package of solutions and tailored products/services».

In the same direction the Italian legislation moves. At the end of 2012 Italy has intervened to facilitate the debt instruments' issuance for SMEs (mini-bonds, commercial papers, project bonds, equity crowdfunding). In fact, with the "Decreto Sviluppo" (decr. Legge n. 83/2012) and "Decreto Destinazione Italia" (decr. Legge n. 145/2013), they have eliminated fiscal constraints that hindered the debt capital issuance by companies not listed on a stock exchange. The lawmaker's goal was to diversify the sources of financing for SMEs in order to reduce the credit crunch and their financial dependence from the banking system. Thanks to the new legislation SMEs, but not "micro-companies", are allowed to issue debt instruments with short-term (commercial paper), medium and long-term (mini-bond, project bond, equity crowdfunding).

It is clear that small banks have objective limits (cultural, skill and equity limitations) in order to start immediately business lines re-entering in corporate banking, that can count on significant income flows.

But, on the other hand, they cannot remain passive and motionless in front of demands of change coming from their main customer, that is the world of SMEs.

In this sense, local banks must necessarily create shared tracks with other banks that are in the same situation by speeding up system initiatives and at the level of association to which they belong or to fix relationship of collaboration and/or partnership with specialized institutions. Whatever the solution to adopt is, there is no doubt that local banks must play a role in the development of financial services to businesses in Italy. This can be implemented if that issue will be faced in an accurate, careful manner and apply proper and functional models in accordance with the role of local bank and the environment where banks and firms operate.

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