

**Authors**

Antoinette Schoar  
Massachusetts Institute of Technology

**The Personal Side of Relationship Banking**

Antoinette Schoar<sup>1</sup>

**Abstract:**

This paper documents a widely overlooked dimension of relationship lending: the personal interaction between the borrower and the lender reduces the willingness of the borrower to engage in moral hazard and default on the loan officer. We conduct a randomized experiment with small business borrowers of the largest commercial bank in India to test the impact of three different levels of interactions between the borrower and the bank. Borrowers who are regularly called either by a single assigned relationship manager or by one manager randomly selected from a small team of managers shows much better repayment behavior and greater satisfaction with the bank services than borrowers who either receive no follow up or only receive follow up calls from the bank when they are delinquent. The results are economically and statistically significant: borrowers who receive the more intensive treatment see a large reduction in the number of late payment spells and delinquencies.

<sup>1</sup>Michael Koerner '09 Professor of Entrepreneurial Finance, MIT Sloan School of Management, NBER and idross2, email: [aschoar@mit.edu](mailto:aschoar@mit.edu). I thank Eduardo Moroya, Max Corner, Matt Chitharanjan, and especially Sharon Butera for outstanding research assistance. I thank Nitai Bargman, Raj Iyer, Sandhil Mullainathan and Jeremy Stein for very helpful comments. The Small Enterprise Finance Centre at the Institute for Financial Management and Research in Chennai, India provided financial support. All errors are my own.

# The Personal Side of Relationship Banking in India

This paper documents a widely overlooked dimension of relationship lending: the personal interaction between the borrower and the lender reduces the willingness of the borrower to engage in moral hazard and default on the loan officer. We conduct a randomized experiment with small business borrowers of the largest commercial bank in India to test the impact of three different levels of interactions between the borrower and the bank. Borrowers who are regularly called either by a single assigned relationship manager or by one manager randomly selected from a small team of managers shows much better repayment behavior and greater satisfaction with the bank services than borrowers who either receive no follow up or only receive follow up calls from the bank when they are delinquent. The results are economically and statistically significant: borrowers who receive the more intensive treatment see a large reduction in the number of late payment spells and delinquencies.

January 01, 2012