As expected, interest rates charged to business in the United States also fall with the size of loans; however, they apparently do not fall as quickly as does the cost of loans. For the year under study, 1979, the normal inverse relationship between interest rates charged and size of loan tended to compress and even reverse itself. In 1979 and again in 1981, small loans were actually being charged lower interest rates than larger loans.[21] One explanation offered by the author of that study was the fact that large borrowers tend to rely on bank credit only irregularly, while small firms are traditionally dependent on banks for financing. American banks thus felt they could discriminate against larger firms since they did not have to cultivate long-term relationships as is the case with smaller firms. In addition, the existence of deposits with interest rate ceilings provided some low cost funds which could be used to keep small business loan rates relatively low.

However, the phenomenon discussed above can also be explained by other factors. Large loans are much more likely to be made on the basis of floating interest rates, while smaller loans are more often at fixed rates. As a result, large loans would react more quickly to rising rates than smaller loans. In other respects, such as the use of collateral, these comparisons are not made among homogeneous loans. Moreover, there is some evidence to suggest that part of the credit rationing imposed by banks was on the basis of quantity rather than price. Small borrowers may have received loans at rates below what their characteristics would normally dictate; but they were restricted in the availability of credit.

Collateral requirements imposed by banks vary greatly by size of borrower. On the basis of a survey of Canadian bank loan files, it was calculated that the average amount of collateral pledged on business loans was 279 per cent of the loan, of which 2/3 was personal collateral.[22] The amount of required collateral was inversely related to firm size; the largest class of firms typically pledged 200 per cent of the loan amount as collateral, while new firms were pledging over 400 per cent of the value of the loan in collateral. The smaller firms also tended to pledge a higher proportion of personal collateral than the larger firms. American statistics tend to support these qualitative conclusions.

Collateral requirements have increased substantially in the past year, according to testimony before the Committee. Part of the reason for this may be that the bank manager and the borrower put a different value on pledged assets; the current recession has done much to reduce the value of certain business assets.

There is no evidence to suggest that the banks' valuations of collateral differ strictly on the basis of loan size or size of borrower. Where companies pledge fixed assets as guarantees, the banks' valuation as a ratio of book value varies little. For the most part, small borrowers are required to pledge more collateral because of higher risk and the lower quality of their assets. In the United States, large loans are far less likely to be secured by collateral than small loans. Moreover, the use of collateral has been increasing since 1977 for small loans while its use has decreased for large loans.[23]

Despite the high levels of collateral pledged against loans to small business, banks are still subject to considerable loss at time of default. Banks were found to recover only 38 per cent of the value of collateral, estimated at the last review. This ranges from a low of 15 per cent on personal collateral to a high of 81 per cent on fixed business assets. Overall, banks tend to recover only 23 per cent of the outstanding value of loans in the case of default. The