

# The Method of "Principled" Negotiation

## How To Build Up Partnership Between Banks and SMEs

### Introduction

Negotiations between banks and small and medium-sized enterprises frequently bring out the tension between trust and partnership spirit on the one hand, control and financial constraints on the other hand.

In order to restore their profitability, many banks had to redesign their credit policy during the last years; i.e. standardizing credit review and approval processes, disconnecting customer relation management and credit approval, introducing risk-based pricing, etc. From the point of view of banks, this approach should contribute to stabilize the financial situation of borrowers. Therefore, it should be in the interest of both the companies concerned and the economy at large.

Small and medium-sized companies often see things differently. On the one hand, they are aware that they cannot afford unprofessional and weak financial management under the current circumstances. But on the other hand, the decisions taken by banks with respect to credit requests – especially when they are negative! – may trigger very strong emotional reactions from the entrepreneurs concerned. When told by a bank that their business is too risky, entrepreneurs are often tempted to think that their professional competence is being unduly questioned or even that they are being personally insulted...

It is also important to consider that negotiations about the granting of a loan are usually characterized by a pronounced imbalance of power. First of all, banks have much more information and resources at their disposal than small and-medium sized businesses. Second, the stakes in such a negotiation are much higher for the entrepreneur than for the bank; in some cases, it is even the future of the borrower that is at stake!

Those remarks apply even more so when the negotiation is about recovering a loan from a company that ran into serious financial difficulties. Beyond financial issues, the self-esteem of the entrepreneur often starts to play a critical role. On the other side, banks may complain (rightly so to some extent) about the fact that entrepreneurs become irrational and refuse to take the legitimate interests of the lender into consideration.

### Negotiation strategy

Several studies have shown that some mechanisms regularly transform negotiations into an exhausting and frustrating exercise - however well intentioned and well qualified the parties may be: focusing on narrowly defined positions and trying to sell one's own arguments to the other side; confusing matters of relationship or personal feelings with those of substance; assuming that the size of the „pie“ is fixed and that any gain for one party represents a loss for the other; putting pressure on the other party to obtain concessions (e.g.: "Take it or leave it"); etc.

According to the method of principled negotiation developed in the framework of the [Harvard Negotiation Project](#), it is far more effective:

- \* to separate the substantive issues from the problems related to the people involved or their relationship; to deal with both, but independently;
- \* to focus on the underlying interests and not on bargaining positions;

- \* to invent options for mutual gain, brainstorming first and then deciding;
- \* to negotiate on the basis of "neutral" criteria (i.e., fair standards and procedures, justifiable considerations, etc.), instead of trying to resolve conflicts of interests by putting the other party under pressure;
- \* to consider one's best alternative to a negotiated agreement before taking any major or final decision in a negotiation, and to think about the alternatives of the other party.

Many people find it difficult to defend their legitimate interests and – if needed – to say no in a way that does not bring a negotiation to a standstill. They may either try to be perceived as acting purely rationally or to put forward a "company policy" (in the present case: a credit policy). However, such a strategy does not work for banks which want at the same time to establish a climate of openness, mutual trust and partnership. Quite clearly, the challenge for them is to be hard on the substance and soft on the people.

The ability to apply the method of principled negotiation would go a long way in helping banks and entrepreneurs to develop good business relationships and resolve conflicts when they arise.

In some cases, the assistance of a negotiation process consultant as trainer, coach, facilitator or mediator may be worthwhile to consider.