Trust in Financial Markets: the role of the human element

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Abstract. The successive financial scandals involving important players in financial markets (Rezaee, 2005) lead the regulators to frantically produce new regulations aimed at preventing such scandals, seeking to increase security and overall trust in the financial system (Barth, Caprio and Levine, 2004). In short, such regulations are based on minimum values for capital ratios, supervising practices, market discipline in close connection with information disclosure, and incentives to adopt "best regulatory and supervisory practices". While there is no guaranteed that the current level of rules and restrictions leads to a more secure financial system (Santos, 2001), it is even less clear that it guarantees an increase in investors’ trust. In fact, such rules – e.g. Basel Core Principles for Effective Banking Supervision (BCPs) or the various Financial Sector Assessment Programs (FSAPs) – tend to affect the performance of financial institutions (Chortareas et al., 2012) affecting also its employees – who are the natural interface between institutions and their clients – and the main drivers of investors’ trust in the system.

In such context, this research suggests that this regulatory growth leaves a fundamental target aside - the human element - essential if one aims at increasing investors’ trust. This work suggests trust is key for investments, adding that trust is even more important when the interaction between the client and the financial institution is usually carried out with a high asymmetry of knowledge about the issues addressed (Corritore, Kracher and Wiedenbeck, 2003; Jarvenpaa, Tractinsky and Vitale, 2000). Based on answers from 366 questionnaire respondents, we use fuzzy set qualitative comparative analysis (fsQCA) to test the conditional arguments that leads the client from a bank to trust his financial advisor. We analyze to which extent the conditions for trust (Butler, 1991) differ between people with different degrees of relationship with the financial markets. To Butler’s conditions, it is added the predisposition to trust (Yamagishi and Sato, 1986). The relationship of each respondent with financial markets is classified as (i) basic - savings / loans and deposits, or (ii) advanced – for the ones that invest directly or through specific products in the financial market. In line with the ongoing development of financial literacy programs worldwide, we also control for the level of financial literacy (Van Rooij, Lusardi and Alessie, 2011a) of respondents. To the best of our knowledge this is a first attempt to introduce Butler’s trust scale and fsQCA in the context of financial markets trust.

We can conclude that trust conditions depend on the type of relationship - basic or advanced. In addition, we notice that financial literacy itself has a non-negligible role in trustworthiness of the investor / financial advisor relationship. In this way, the consideration of the human element into the strategies to strengthen confidence in the financial market seems a promising venue. Knowing those differences, allows us to suggest qualitative improvements of the relationship between financial institutions and their clients and a better understanding on how to improvement of trust in financial market.

Keywords: Banking Regulation, Trust, Financial Literacy, fsQCA.

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References


