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WHICH BANKS DO RUSSIAN HOUSEHOLDS (DIS-) TRUST MORE?

Introduction

The objective of this paper is to find out which banks the Russian households trust more and whether they really prefer to keep their savings in the institutions that they verbally prefer. It is an interdisciplinary study in the sense that we examine data from sociological polls and then try to compare it to banking statistics.

The motivation for this study came from the sociological literature on the phenomenon of trust [Ennew, Sekhon, 2007; Ibragimova, 2012] as well as from the econometric studies of the behavior of depositors and the effects of deposit insurance [Anginer, Demirgüç-Kunt, Zhu, 2014; Karas, Pyle, Schoors, 2013].

Data and methodology

There have been five waves of the monitoring of Russian households' financial behavior (2009–2013), in which two of the authors of this paper were involved. It is a nation-wide survey based on face-to-face interviews at the place of residence. The survey is held yearly in the 4th quarter and embraces a stratified sample of adult people (18+) representative in terms of age, gender, education level, residence, and federal district. The most recent survey took place in 42 regions and 140 settlements. $N = 1600$, and sample error is 3.4 percent. The polls included a number of questions meant to feature the degree of respondents' trust towards various financial institutions in Russia (banks, insurance companies, pension funds, mutual funds and credit cooperatives).

The Russian banking statistics that we use comes from banks' disclosure published by the Central Bank of Russia and consisting of monthly bank-level data for 2004–2014.

Sociological literature suggests that trust has a cognitive dimension based on a sort of rationale and an affective dimension related to one's beliefs [Ennew, Sekhon, 2007]. In order to find out which type of trust underlies the attitude of Russian citizens towards banks we test the influence of financial literacy and capability on the

level of trust to banks. If financial literacy and trust to banks are positively correlated, we consider it as a manifestation of cognitive dimension of trust. If there is a negative relationship, i.e. the high level of trust is conditional on low level of financial literacy, then it supports the hypothesis of an affective dimension of trust to banks. We test the hypotheses that trust to state-controlled banks is mostly affective whereas trust to privately owned commercial banks is mostly cognitive.

We perform a principal component analysis to determine which financial institutions enjoy higher level of trust and what the drivers of that trust level are.

Trust to banks from a sociological viewpoint

Within the fifth wave (2013) of the monitoring of Russian households' financial behavior, we collected responses with regard to specific types of financial institutions (Fig. 1). Predictably, people tend to trust more the Sberbank of Russia followed by other state-controlled banks, while there is broad distrust of privately-owned financial intermediaries regardless of other characteristics. Sberbank firmly leads in terms of the balance between positive and negative response (+29). 72 percent of respondents trust Sberbank while only 23 percent do not. State-controlled banks other than Sberbank are neither trusted nor distrusted, which is a surprising outcome in view of the fact that legal status and the risk profile of these banks are not much different from those of Sberbank.

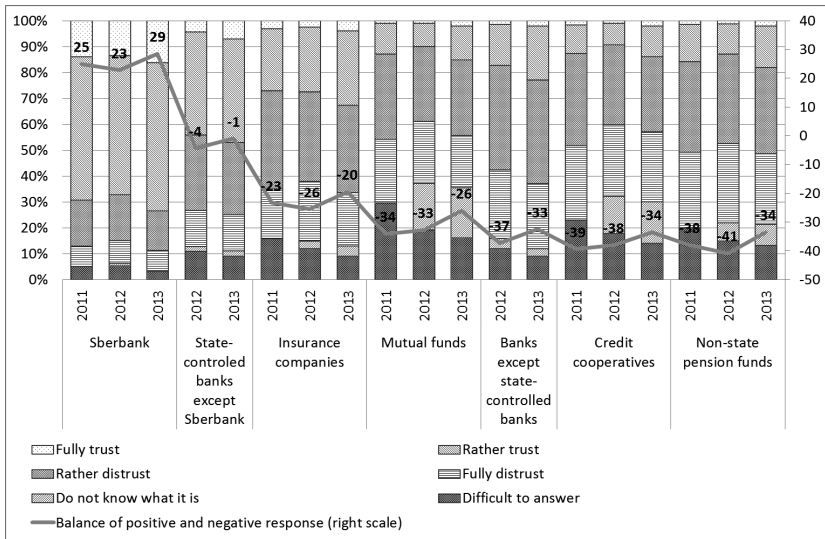


Fig. 1. Level of trust in different types of financial institutes, % of all respondents
Source: Monitoring of Russian households' financial behavior, HSE 2013.

The survey demonstrates that even though privately-owned commercial banks are trusted more than credit cooperatives in absolute terms (23 percent of Russians trust these banks as compared with 14 percent of Russians who trust credit cooperatives in 2013), a critically low level of trust of the population towards privately-owned commercial banks was revealed among those who are informed of what credit cooperatives and privately-owned commercial banks are. Quite unexpectedly, households expressed almost the same degree of trust towards this type of banks and towards credit cooperatives (a negative balance of responses at -33 for privately-owned commercial banks as compared with -34 for credit cooperatives), despite the burgeoning evidence of loan-sharking, unsustainable rates and obscure business practices of the latter. This result casts doubt over the rationale and the effectiveness of government regulation of the banking sector since unregulated intermediaries (credit cooperatives and microfinance lending institutions) enjoy a similarly low level of trust.

During 2012–2013 the dynamics of change in trust is positive for all categories of financial intermediaries without exception. We attribute this result to the well-known effect that shifts the balance between greed and fear depending on the specific point of the economic cycle. 2012 has been generally a good and stable year for the Russian economy, so households show increased trust to financial intermediaries across the board.

We then compare the sociological results with data coming from banking statistics on household deposits. There appears to be a deep mismatch because the market share of Sberbank has actually fallen within the period of observations, and the pace of increase in the volume of deposits at private institutions has been high enough with regard to the declared low level of trust in them. After some econometric processing and analysis we tend to explain this phenomenon by the effects of the deposit insurance system. A statistically strong correlation between the level of coverage in the Russian deposit insurance system and the inflow of deposits into privately owned banks is interpreted as deterioration of market discipline in the deposit market and an enhancement of moral hazard. Depositors care less and less about the banks they invest in. This effect might even be stronger than the flight to quality that usually occurs in during a crisis: the traditional wake-up call effect of a crisis is muted by the numbing effect of deposit insurance [Karas, Schoors, Pyle, 2013]. We thus suggest that the state-run deposit insurance system artificially keeps afloat the private deposit-takers by offsetting the (well-deserved) distrust of Russian households. We try to model what the structure of Russian household deposits market would look like in the absence of deposit insurance.

Drivers of trust towards different types of banks

In this study, we explore the structures of trust in institutions using the questions to what extent our respondents trust or distrust social and financial institutions:

TV, police, courts, government, parliament, president, state regulators of financial sector (Central bank, Federal financial markets service and Deposit insurance agency) and different types of companies in financial services industry (Sberbank, other state-controlled banks, all other banks, insurance companies, mutual funds, credit cooperatives and private pension funds). Using principal component analysis we aggregate manifest measures of trust into three latent factors: trust in social and political institutions, trust in private sector financial institutions which also includes trust in State deposit agency and trust in state regulators of financial sector and state banks. The results of principal component analysis are presented in the Annex 1.

Trust in social and political institutions that explains 28 percent of variation consists of such items as government, parliament, president, courts, police and TV. The trust in private sector financial institutions that explains 26 percent of variation correlates with trust in non-state banks, credit cooperatives, mutual funds, private pension funds and insurance companies, as well as with trust in State deposit agency which protects money deposited in retail banks. Trust in state regulators of financial sector and state banks that explains 18 percent of variation is linked to trust in Sberbank and other state-controlled banks, as well as trust in state regulators such as the Central Bank of Russia and the Federal Financial Markets Service (merged with the CBR in 2010).

Factor scores were generated for each respondent on these three trust dimensions. We find that these latent factors are differently manifested across social and demographic groups of respondents. The group of young adults has relatively higher scores on trust in private sector and state-controlled financial institutions, whereas in older adults group these types of trust reach a minimum (Annex 2, Fig. (a)).

Across settlement status groups, trust in state banks and state regulators increases with the number of people who dwell in a settlement: the highest scores are revealed in the large megacities, the lowest — in rural villages (Annex 2, Fig. (b)).

Users of financial services (those who use salary cards and any other financial products) differ from non-users (those who do not use financial services or use only salary cards) on dimension of trust in state banks and state regulators only. Users of financial services have higher scores in this dimension of trust as opposed to non-users (Annex 2, Fig. (c)).

To what extent trust in financial institutions is associated with financial literacy? Financial literacy according to OECD/INFE¹ definition is “a combination of awareness, knowledge, skill, attitude and behavior necessary to make sound financial decisions and ultimately achieve individual financial wellbeing”. Will more financially literate people have more trust in financial institutions? Or “a lot of knowledge — a lot of sadness”, i.e. the awareness of the pros and cons of financial markets will make people take financial institutions with a grain of salt?

¹ OECD International Network on Financial Education.

To measure levels of financial literacy, we designed a set of four survey questions. Those questions reflect four basic concepts of financially responsible behavior and basic understanding of the ABCs of finance: a) signing contracts only after reading and a complete understanding of its terms; b) keeping a written record of incomes and expenses; c) knowledge of which financial assets are insured by the state; g) understanding of the relationship between risks and rewards. Our data shows that those who are financially literate have higher scores on trust in state banks and state regulators. Differences in other dimensions of trust are not statistically significant. (Annex 2, Fig. (d)). Those who are able correctly answer the question on the state deposit insurance system, are more likely to have higher scores on trust in non-state banks. And on the contrary, those who do not know about this system are more likely to trust in state banks believing that only the state’s ownership of the bank can guarantee them the safety of their deposits (Table 1).

Table 1. Awareness about the state insurance system across the groups with trust in different types banks, column %

	Which assets are insured by the state?		Total
	wrong answer	right answer	
Trust state banks	72	63	70
Trust private banks	28	37	30
Total	100	100	100

Source: Monitoring of Russian households’ financial behaviour, HSE 2013.

Consistency between sociological findings and banking statistics

We then proceed to check the consistency between the outcomes of public opinion polls and the Russian banking statistics. Our hypothesis is that there is a mismatch in the change of feelings towards different types of financial intermediaries over time and the dynamics of household deposits.

Banking statistics suggest that Sberbank, the main holder of Russian private deposits, has been losing market share in 2004–2014 (Fig. 2). While this decline was partly offset by the expansion of other state-controlled banks, all state-controlled banks taken together have been losing ground, except for a short period of confidence crisis and flight to quality in 2008 and the recent correction in 2013–2014. What strikes us most is that from 2011 through 2013 the pronounced trust of Russian households in Sberbank increased and their trust in private banks fell (Fig. 1), but the actual deposit flows tended to have the opposite direction.

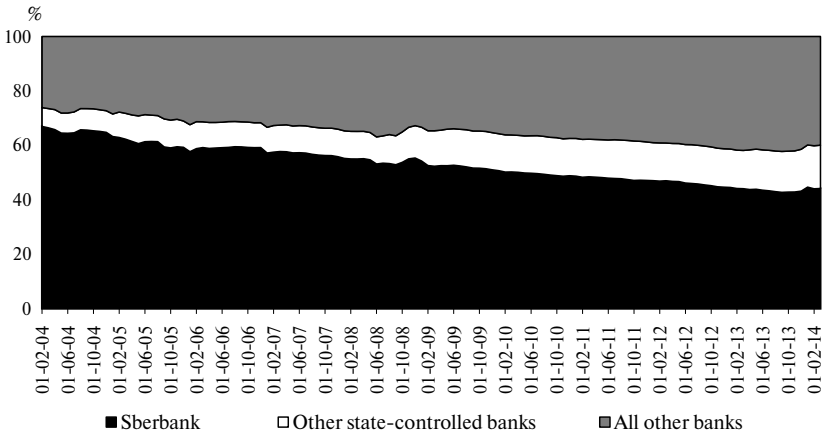


Fig. 2. The structure of the Russian market for household deposits

Source: Calculated on the basis of CBR data. State-controlled banks as defined by [Vernikov, 2009; 2012].

Our interpretation of this finding relates to the effects of the deposit insurance system that was introduced in Russian in 2004. If Russian households quite clearly indicate that they do not trust private banks but still are prepared to restructure their savings in favor of those banks, then it is the merit of the deposit insurance and not those banks. Essentially who people trust are government institutions at large regardless of the degree of awareness about the details of the deposit insurance system or the mere existence of the Deposit Insurance Agency (*ASV*).

Conclusions

Our findings can be summarized as follows.

Poll results are tested by banking statistics on household deposits and get an overall validation. Russian households traditionally trust state-controlled banks and particularly the national champion (Sberbank) at the expense of privately owned deposit-taking institutions. The gap in the level of trust between state-controlled banks and all others remains deep and unlikely to disappear. This effect diminishes over time mainly to the market-discipline eroding impact of deposit insurance. During the period of healthy economic growth the issue of trust becomes less relevant than during financial turmoil. The more disaggregated the analysis of Russian banking becomes, the more sensible results it yields.

Our findings confirm the need for a disaggregated analysis the Russian banking sector. It also appears that private financial intermediation in Russia has shaky foundations in view of the lack of general trust that has changed little over the past years.

The very low and declining degree of trust in other than state-controlled banks suggests that there is little hope in self-sustaining business of those banks that would rest on the inflow of private savings at reasonable rates. The policy implication of this finding is that the authorities will face the dilemma of ever increasing the level of private savings protection under the deposit insurance scheme (as well as the resulting public costs) in order to keep the smaller market participants afloat, or give up on the idealistic drive to artificially enhance competition in the household deposit market.

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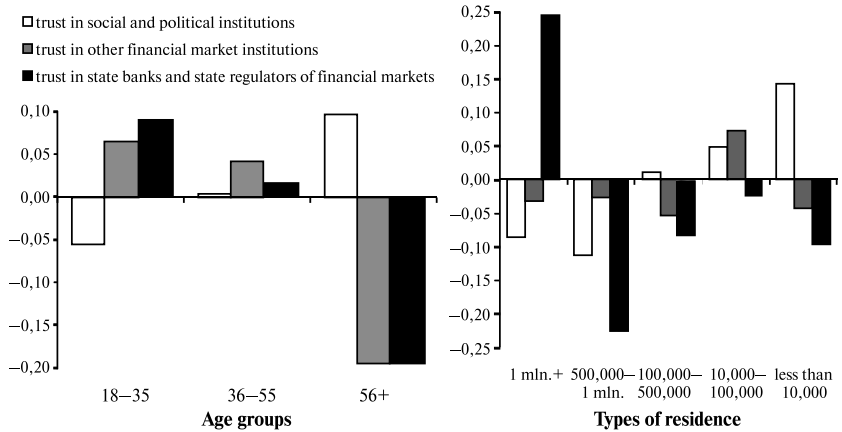
Annex 1. Principal component analysis: Rotated Component Matrix

<i>Q.</i> : Do you trust or distrust the following institutions?	1	2	3
TV	0.660		
Police	0.801		
Courts	0.779		
Government	0.837		
Parliament	0.810		
President	0.732		
Deposit Insurance Agency		0.620	
Non-state-controlled banks		0.681	
Insurance companies		0.684	
Mutual funds		0.838	
Credit cooperatives		0.870	
Private pension funds		0.766	
Central bank			0.733
Federal Financial Markets Service			0.514
Sberbank			0.841
Other state-controlled banks			0.694
Variation explained,%	28	26	18

1 — fully distrust; 2 — somewhat distrust; 3 — somewhat trust; 4 — fully trust.

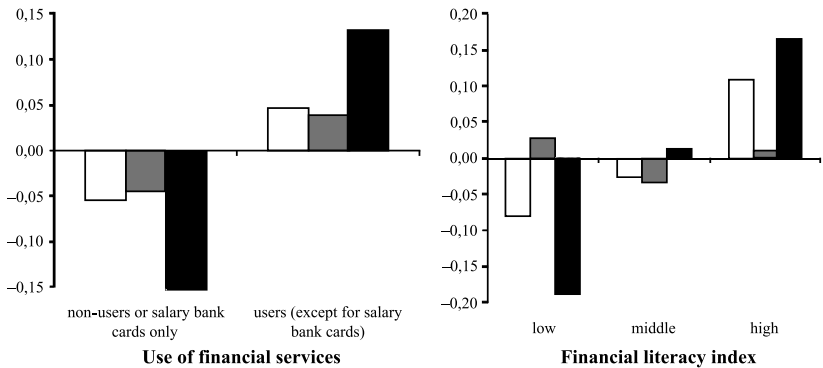
Source: Monitoring of Russian households' financial behaviour (2009–2013).

Annex 2. Drivers of trust in financial institutions



(a) Trust in institutions across age groups

(b) Trust in institutions across types of residence



(c) Trust in institutions across users and non-users of financial services

(d) Financial literacy as a factor of trust of financial services