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Bank Run Psychology

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Highlights

- We experimentally show that background emotional state has a large significant effect on withdrawals in an experimental bank run game.
- In particular, the presence of background fear among subjects greatly increases the likelihood of withdrawal behavior that results in a bank run scenario.
- Women are more likely to withdraw than men but only when they have been induced with a background emotional state of fear.

Abstract

Banks are inherently susceptible to panics and bank runs due to the problem of maturity mismatch, resulting in both a stable equilibrium in which the bank survives and an unstable equilibrium in which a bank run occurs. Understanding equilibrium selection in this setting is extremely important for safeguarding financial stability. In this paper one new potential factor that determines whether a bank runs gets triggered or not is experimentally studied, namely the psychological state of the depositor. Prior to participating in an experimental bank run game, subjects are either induced with fear, sadness or happiness using an autobiographical emotion induction task. The findings suggest that the presence of background fear significantly increases the likelihood of withdrawal and a subsequent bank run. In addition women are shown to be significantly more likely to withdraw than men, but only in the fear induction treatment.

Keywords: Bank runs; Contagion; Emotions;

JEL: D70, G02, G21

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