



Knowledge and opinions about banking supervision: Evidence from a survey of Dutch households

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ABSTRACT

What does the general public know about banking supervision? What objectives does the public think bank supervisors should pursue? We investigate these issues using a survey among Dutch households. First, we find that the public's knowledge about banking supervision is far from perfect. We also find that respondents often expect more from supervisors than they can realistically achieve. Finally, our findings suggest that better-informed people have more realistic views on banking supervision. Realistic views on banking supervision lead to more prudent financial behavior, which, in turn, contributes to financial stability. Therefore, the communication policies of banking supervisors should aim to improve the public's knowledge about banking supervision.

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1. Introduction

When the financial crisis struck the world economy, several banks failed. In other cases, financial institutions needed government support in order to survive. The authorities responsible for banking supervision came under criticism. Although some authors have expressed doubts about the effectiveness of banking supervision (Demirgüç-Kunt and Detragiache, 2011), several efforts have been taken to enhance banking supervision.¹

Public reactions to recent bank failures suggest that at the time, many people were unaware of the risks occurring in the financial sector (Nofsinger, forthcoming). Individuals who underestimate

such risks are more likely to take sub-optimal financial decisions. If the supervisor is blamed for the failure of a financial institution, this may harm the supervisor's credibility, and hence its effectiveness. Indeed, after some banks in the Netherlands had failed, public confidence in De Nederlandsche Bank (DNB)² dropped, from 91 percent in 2006 to 72 percent in 2010. If based on unrealistic expectations, confidence in supervisors (and financial institutions in general) will be affected during financial turmoil.³

It is therefore important for supervisors to understand what people know about banking supervision and what they expect supervisors to do. If the level of awareness is low, or if expectations are over-optimistic, the supervisor may want to address these gaps

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¹ For instance, the Basel Committee on Banking Supervision has put forward far-reaching proposals (Basel III); see <http://www.bis.org/bcbs/basel3.htm>. See also Goodhart (2008) and Dewatripont et al. (2010) for a discussion on lessons drawn from the financial crisis. For an assessment of EU and national authorities' response to the financial crisis, see Pisani-Ferry and Sapir (2010).

² De Nederlandsche Bank is the central bank of the Netherlands and is responsible for micro-prudential supervision of banks, insurance companies and pension funds.

³ As noted by one of the referees, even with more realistic expectations, the extent of the financial turmoil was likely to shake the public's confidence. Still, we argue that it is better if the public is aware of what supervisors can and cannot realistically deliver. Especially during uncertain times, a large confidence shock may exacerbate the crisis. See also Mosch and Prast (2008) for empirical research on confidence in the financial sector.

in the public's knowledge. In this paper, we discuss the following questions. First, what does the public know about banking supervision, and how does it obtain its information? Second, what does the public expect supervisors to do? Finally, what drives the public's opinions about banking supervision?

We investigate these issues using the Netherlands as a case study. Three characteristics make the Netherlands an interesting country to study in this context. First, the Dutch financial sector is relatively large, contributing about 7.5 percent to GDP and directly providing employment to about 3.5 percent of the workforce. Second, recent developments in the Dutch financial sector were quite tumultuous. A number of smaller banks went bankrupt and various large financial institutions received government support, in the form of either capital injections or nationalization. Third, the Dutch so-called Twin Peaks model of supervision is widely considered as a benchmark for other countries. Under this model, DNB is responsible for micro-prudential supervision, whereas the Netherlands Authority for the Financial Markets (AFM) exercises market conduct supervision.

This paper is closely related to the literature on financial literacy. Various papers in this field have shown how knowledge about financial issues is related to decision-making. For instance, Lusardi and Mitchell (2007) and van Rooij et al. (2011a) find that more knowledgeable people are also more likely to plan for retirement. Likewise, van Rooij et al. (2011b) conclude that people of low literacy are less likely to invest in stocks. As far as we know, our paper is the first to investigate knowledge and opinions about banking supervision. One closely related paper is van der Cruysen et al. (2010) who report that knowledge on the ECB's monetary policy contributes to an individual's ability to form realistic inflation expectations.

To organize our analysis, we use the framework proposed by Blinder and Krueger (2004) in their study on the determinants of opinions on U.S. economic policy. This framework links various factors, which influence opinions and knowledge, such as people's willingness to be informed, the sources they use, the type of job they have, and their level of education. We use data from the DNB Household Survey (DHS), a continuous internet-based survey among Dutch households. We presented participants with thirteen statements about the responsibilities of banking supervisors in the Netherlands, asking them to indicate whether the statements were true or false. The number of correct answers is used to construct a proxy for knowledge. Likewise, we asked our respondents what they thought supervisors should do, in order to create a proxy for opinions.

Our main findings are as follows. First, perhaps unsurprisingly given the complexities of financial supervision, knowledge about micro-prudential supervision is far from perfect. Less than 15 percent of the respondents answered more than half of the knowledge questions correctly. Second, respondents often expect more from supervisors than they can realistically deliver. For instance, three out of five respondents indicated that it should be the task of supervisors to prevent all bankruptcies. Finally, our results suggest that better knowledge about supervision is related to more realistic opinions. As realistic views on banking supervision lead to more prudent financial behavior, thereby contributing to financial stability, communication policies of banking supervisors should aim to improve public knowledge about banking supervision.

The remainder of the paper is structured as follows. Section 2 sets out the methodological framework, while Section 3 presents the outcomes of the survey. Sections 4 and 5 outline our proxies for knowledge and opinions about banking supervision, respectively. Section 6 presents results based on ordered probit models. The final section offers the conclusions and policy recommendations.

2. A framework for the analysis

Opinions about banking supervision are probably related to knowledge on the subject, which, in turn, depends on a number of factors. First, there are the benefits expected from acquiring information. Someone who sees no advantage in being informed about financial supervision will have little incentive to obtain the relevant information, so that their level of understanding will remain low. Second, given that someone does have an interest, the sources of information may become relevant. Most people do not receive their information about banking supervision directly from the supervisory authority but rather through 'intermediaries' such as television, radio and newspapers. Third, the intensity with which a particular media source is used is likely to matter for a person's knowledge and opinions about banking supervision. Finally, several other variables, such as level of education, type of job or income level, may also be relevant.

All these factors are interrelated. To formalize the interdependencies between opinions (O), knowledge (K), desire to be informed (D), and intensity of information (Q), we use a framework similar to the one proposed by Blinder and Krueger (2004). Our basic model is:

$$O_i = f(SI_i, K_i, ED_i, X_i) + e_{1,i} \quad (1)$$

where SI is self-interest, ED is education, and X is a vector that contains control variables such as gender, age and location. A person's knowledge about supervision depends on their educational background as well as their desire to be informed. And the sources of information and the intensity of information used (Q) may also affect K . Finally, K depends on various control variables too. Thus we may write,

$$K_i = g(ED_i, D_i, Q_i, X_i) + e_{2,i} \quad (2)$$

Following Blinder and Krueger (2004), we further posit that:

$$Q_i = h_1(D_i, SI_i, ED_i, X_i) + e_{3,i} \quad (3)$$

The sources of information and the intensity of their use depend on the desire to be informed, self-interest, education, and various control variables. The stronger a person's wish to be informed about banking supervision and the stronger the self-interest, the more (different) sources of information they will use and the more information will be acquired. Finally, the level of education is also likely to affect the intensity of the sources used to get information. First, highly educated persons will read different newspapers than people with low levels of education.⁴ Also, they may attach more importance to newspapers than to, say, television. Second, individuals with lower degrees of education may use fewer sources of information. Third, there is evidence that the level of education matters for the diversity of media sources used. For instance, Grabe et al. (2009) show that highly educated persons tend to be better at remembering items read in newspapers and on the internet. By contrast, the lower educated perform best in recalling news presented on television.

The desire to be informed depends on self-interest, education and various covariates. Self-interest may be relevant for several reasons. For example, individuals with savings have strong interest

⁴ van der Cruysen et al. (2010) gathered information on the specific newspapers used by respondents to obtain information on the European Central Bank. They find a clear relationship between levels of education and newspaper readership. Newspapers that are perceived as "high-brow", like *NRC Handelsblad* and *De Volkskrant*, were more likely to be read by people with higher levels of education. A more popular newspaper like *De Telegraaf* was read by less well-educated respondents. See also Chan and Goldthorpe (2007).

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