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Researchers Find Lack of Trust in Leaders, Institutions Is Major Factor in U.S. Economic Crisis *New Chicago Booth/Kellogg School Financial Trust Index Measures National Confidence in Financial System*

CHICAGO (Jan. 27, 2009) - As unemployment rates rise, the housing crisis deepens and 401Ks continue to deplete, it should come as no surprise that America's trust of its financial leaders and institutions has plummeted. To study the financial implications of eroding trust, Paola Sapienza (Kellogg School of Management at Northwestern University) and Luigi Zingales (University of Chicago Booth School of Business) have created the Chicago Booth/Kellogg School Financial Trust Index, publishing the first wave of results today. The accompanying research shows just how deep America's declining trust runs and how strongly it contributes to the country's financial problems.

"Trust is a powerful motivator of economic behavior," said Sapienza, "Our previous research and anecdotal evidence suggest that lack of trust can have paralyzing effects on financing and investments. We developed the Financial Trust Index to measure this often ignored economic indicator and gain insight into how the government's reaction affects the economy."

The Financial Trust Index will measure public opinion every three months to track changes in attitude over time and will provide a better understanding of public trust, the absence of which, according to Sapienza and Zingales, can bring even the richest, most advanced economies to a grinding halt.

FINANCIAL TRUST INDEX: KEY FINDINGS

Seeking to formalize the relationship between trust and finance, Sapienza and Zingales analyzed data from more than 1,000 American households, randomly chosen and surveyed via phone over two weeks in late December, 2008.

- Sapienza and Zingales found that only 20 percent of those surveyed currently trust the financial system.
- Only 11 percent of people trust the stock market. This trust is a strong predictor of individuals' intentions to increase or decrease their investment in the stock market over the next few months.
- Similarly, they found that 11 percent of the respondents withdrew money from the bank and kept it in cash during the crisis. This behavior is highly correlated with the individuals' trust for banks.
- They also found that trust in the financial sector has declined sharply over the last few months. When asked how their trust had changed over the past three months, respondents indicated a decrease across all categories, with perceptions of the stock market most soured.

One of the goals of this research was to determine to what extent (if any) the perception of current events and government policy impact the trust people have in financial markets.

- Respondents who identify the main cause of the 2008 financial crisis as lax government oversight (16 percent) or regulation (15 percent) exhibit the least trust in the market.
- Levels of trust were also low among those who blamed companies, citing poor corporate governance (15 percent) or managerial greed (36 percent).

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While the heavy financial losses suffered can in part explain this reduced trust, a crucial factor seems to be the way in which the government has intervened.

- While the majority of respondents favor government intervention in financial markets, 80 percent said the way it intervened has made them less confident in the market.
- Even among the respondents who felt that federal intervention in the financial sector should increase, 75 percent still lost confidence as a result of recent federal intervention. This percentage rises to 95 percent among those who did not favor government intervention.

In other words, even among investors who are ideologically favorable to government intervention in financial markets, three out of four have been made less confident by the way the government has intervened.

"One of the key factors undermining trust," said Zingales, "is the perception that the rules have changed in the middle of the game. The government has done exactly this. What is most shocking is how deeply this has affected the trust of the average American."

Further questions proved that "coziness" between government and the financial industry, whether real or perceived, is clearly a problem in the eyes of many Americans. Respondents were asked to choose what motivated former Treasury Secretary Henry Paulson as he engineered and executed the government response. While 20 percent of respondents had no opinion, the remaining 80 percent were evenly split. Half the group, 40 percent of the overall respondents, believed Paulson acted in the interest of the country. The other 40 percent, however, believed that Paulson's plan was meant to benefit Goldman Sachs, the investment bank at which he served as chairman and CEO prior to being appointed Secretary.

ABOUT THE SURVEY: The survey was conducted by Social Science Research Solutions (SSRS) using ICR's weekly telephone omnibus service. Exactly 1,034 individuals were surveyed over two weeks starting on December 17, 2008. A fully replicated, stratified, single-stage random-digit-dialing sample of landline telephone households was used to identify survey subjects. Within each sample household, one adult respondent was randomly selected using a computerized procedure based on the "Most Recent Birthday Method" of respondent selection. Once a respondent was contacted, he or she was asked if they are the main or joint financial decision makers in the household. Only individuals replying positively to this question were surveyed.

MORE INFORMATION: To see the full study, visit www.financialtrustindex.org. To arrange an interview, contact Meg Washburn or Barbara Backe at the contact information listed above.

To learn more about the Kellogg School of Management at Northwestern University, visit www.kellogg.northwestern.edu.

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