# Trust, Credit Divergence, and Financial (De)Regulation

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## Question

- How does trust affect access to credit and economic growth?
- A model yielding two equilibria
- Empirical analysis with two main results:

1. Distrust predicts less formal borrowing and less credit
2. High-trust countries experience higher economic growth after financial liberalization

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- Two types (by choice): trustworthy and not
- Lenders cannot distinguish – end up offering an average price
- Trustworthy leave to borrow from informal markets
- There is also a good equilibrium, similar to Diamond and Dybvig (1983)
- Financial liberalization benefits in good equilibrium but harms in a bad one

# Empirical results

- Use country-level index of trust
- Countries with high trust borrow less from informal markets
- Financial liberalization (banking) increases GDP growth in high-trust countries
- GDP growth declines in low-trust countries

# Overview of the comments

- Paper's model follows the literature but importantly allows for a choice of the type
- New predictions about the impact of trust on credit markets and economic growth
- My comments:

1. Trust vs other channels
2. Measurement of trust
3. Long-term effects
4. Minor comments

## Comment 1: trust vs other channels

- Not clear if trust is a first-order channel
- Happiness (Stevenson and Wolfers (2008)), development of financial markets (Levine (2005), Durusu-Ciftci et al (2017)), and life expectancy (Acemoglu and Johnson (2007)) would produce similar results on GDP growth
- Evidence on credit in the literature is more mixed but generally in line with the paper
- Separating the effect of trust from other channels is very important, controlling only helps with observables

## Suggestions

- Find exogenous variation in trust. Some ideas:
  - Social ties and trust as in Italy (see Guiso, Sapienza, Zingales (2004))
  - Communism vs capitilism – post-WW2 Germany
  - Armenia after 2018 velvet revolution (or any other country with a peaceful transition to democracy or reverse)
  - Random refugee assignment in Sweden in 1980s

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  - Random refugee assignment in Sweden in 1980s
- Focus on credit rather than GDP growth – more direct and more promising
- Use Altonji et al (2005) sensitivity test to solidify identification through including controls

# Comment 2: measurements

- The model considers people with new accounts or low scores – excluding rationing
- Trust data is country-level and could be mismeasured in low-trust countries
- **Suggestion 1:** include high-score borrowers in the model
  - Will they also move to informal borrowing?
  - Could be problematic to test empirically if the data is country-level
- **Suggestion 2:** exogenous variation to help with measument errors

# Comment 3: long-term effects

- For low-trust countries tighter regulation leads to higher GDP growth
- More tightening can also make the regime more authoritarian, especially in low-trust economies
- Authoritarization does not predict higher stock returns (Miller (2025))
- **Suggestion:** consider long-term consequences of tightening

# Minor comments

- Bank regulations are very specific and they affect lenders more than borrowers
- Not sure how MNP helps with identification
- Talk about how variables are measured early on
- Connect with bank run and global games literature (Diamond and Dybvig (1983), Morris and Shin (1998), Goldstein and Pauzner (2005))
- Family and friends can also trust you less
- Explain more why lenders should think about trust if they have good credit scoring in place

# Conclusion

- Ambitious and thought-provoking paper
- More work to separate trust channel from other channels can help
- Good luck!