Discussion on "Identifying Constraints to Financial Inclusion and their Impact on GDP and Inequality: A Structural Framework for Policy"

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Objective of the paper

This is a policy oriented paper to study the effect of different components of financial inclusion...

- Participation costs in financial markets: ψ
- Collateral constraints: λ
- Intermediation efficiency: χ

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... on GDP, TFP, inequality and welfare

Methodology

Build a heterogeneous agents model to quantify the importance of each feature

- ▶ Two occupations: entrepreneur and worker

- ▶ Two sources of heterogeneity: assets and talent

- ▶ Two financial regimes: savings and credit

- ▶ Two key market features: limited commitment and asymmetric information

Main mechanism

Reallocation of labor and capital into different endogenous categories

- ▶ Workers: unconstrained and constrained
  - ▶ Constrained workers = wannabe entrepreneurs

- ▶ Entrepreneurs
  - ▶ Unconstrained and constrained
  - ▶ Highly leveraged or not

Results

- Reducing participation costs
  - Increase GDP less than 20%
  - Reduces TFP
    - Can we interpret them as efficiency losses? May be not!
  - Inequality is relatively flat
- Relaxing collateral constraints
  - Both GDP and TFP increases
  - Inequality displays Kuznet's curve
- Increasing intermediation efficiency
  - GDP remains flat but TFP increases (through making allocation of capital easier for talented entrepreneurs)
  - Inequality displays Kuznet's curve

Comments

This is a very nice paper that points out that one policy does not fit all. Country specific conditions matter a lot to understand the effects of policy reforms... In this paper... financial inclusion

Comments

There is only one assumption I believe it would be nice to relax...

$$u(c, b') = c^{1-\omega} b'^{\omega}$$

... which implies a constant saving rate of ω...

- ▶ Saving rates are not constant across countries, nor along time

- ▶ Saving rates react to policy changes, even more in a heterogeneous agents model

  - ▶ Functional form implies risk neutrality

... of course this assumption may not affect results qualitatively

Would it be very hard to solve the model with

$$u(c, b') = \left[(1 - \omega)\, c^\rho + \omega b'^\rho\right]^{\frac{1}{\rho}}$$

This change in the functional form solves to extreme assumptions in the paper

- ▶ Constant savings rate
- ▶ Risk neutrality
- ▶ Pretty sure complicates solving the problem of asymmetric information

Other Comments

- A key characteristic of less developed and emerging economies is the large number of self employed people... dos this model capture this feature?

- Some papers find that the effect of financial frictions account for a substantial fraction of cross country differences in GDPpc, relative to the US... This paper find smaller effects, why?

- Model period is a year but there are two generations...
  - This may be important to the assumption that workers may not get paid... does it matter?
- Can it be done for countries that have implemented policies to increase the access to credits?