Financialization, Inequality and Governance

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Abstract

We investigate the pattern and causes of inequality in a large sample of advanced, emerging market and developing economies over the recent decades. The literature often ignores the impact of financialization on the evolution of inequality. Financialization may alleviate the financial constraint of individuals and firms who lack the opportunity to access the financial markets because of too restrictive collateral regulation. Higher financialization levels by enabling to meet financial requirements and investment projects of resource constrained individuals and firms may decrease the inequality. On the other hand, higher financialization levels by leading to economic instability may increase the inequality. In this context, this study suggests that the impact of financialization on inequality is conditional on the institutional quality and governance levels of the economies. This study investigates this crucially important research topic both by employing dynamic panel data as well as panel threshold estimation methods. To this end, we investigate whether institutional quality and governance provide a data-driven threshold for the impact of financialization on inequality for our sample of advanced, emerging market and developing economies.

Keywords: Emerging Market Economies, Developing Economies, Financialization, Inequality, Governance

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