

Does financial liberalization affect the distribution of income between wages and profits ?

by

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Abstract

Neoclassical theory says that financial liberalization will make the cost of capital decrease, productivity increase and output grow. In reality this does not happen. A key to understanding why it is so is the link between financial liberalization and income distribution.

After financial liberalizations both the real interest rate and the supply of credit to the non traded goods sector rise. If the monetary interest rate and the profit rate tend to be equal in the long run, a reshuffling of production favouring the non-traded goods sector will occur; for the mark-up may be higher in this sector than in the traded goods sector due to the lack of international competition. Households, no more credit constrained, will increase their demand for non traded goods; profits in this sector will increase too due to the higher capacity utilization. On the other hand the likely fall in the propensity to save of capitalists will cause a slower capital accumulation. Thus neither investment nor productivity will rise. This may not be due to the working of real forces alone, such as trade liberalization, but rather to the interplay of both monetary and real factors. A vicious circle of lower growth and rising inequality could be set in motion.

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