Financial Intermediation
and Entrepreneurial Activity

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A Non-Technical Summary

This paper studies the effects of financial intermediation on aggregate levels and
the distribution of resources in an economy with wealth-constrained heterogeneous
agents and occupational choice. Whether an agent becomes an entrepreneur de-
pends on a realized entrepreneurial ability and accumulated assets needed to fi-
ance a business project with uncertain returns. I compare a steady state of an
economy with financial intermediation to an economy in which entrepreneurs must
finance their projects only from their savings. The simulated benchmark economy
matches well the U.S. data on the distribution of occupations and resources. The
efficiency and welfare losses in the economy without financial intermediation are
large and since the workers bear most of the adverse effects, the economy is also
more unequal. Finally, a transition from the steady state of the economy with-
out financial intermediation simulates the process of financial development: both
measures of inequality decline monotonically during the transition.