Direct and Indirect Finance and Income Inequality

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Income inequality in Japan has been expanded since early 1990s, which means that the Japanese economy becomes an `unequal' society. It is said that the cause of recent income inequality in Japan is not property income but wage income. If property incomes, such as interest, dividend and rent, are the most important, income inequality in Japan would have depressed after the collapse of the asset bubble economy. However, income inequality in Japan has been increasing since early 1990s. Therefore, property income is not the first-order important.

This paper builds an overlapping generations model incorporating the optimal behavior of the banks and analyzes the relationship between a financial development and income inequality. Our analysis is consistent with recent empirical research, which shows that a financial development reduces income inequality by increasing poors' incomes.

Our model predicts that a negative shock to collateral assets enlarges income inequality through a financial sector. Regarding a negative shock to collaterals as the crash of the asset bubble economy, our analysis is consistent with what the Japanese economy has experienced since early 1990s.