Spring 4-29-2021

How Does Financial Inclusion Affect Firm Performance and Participation in Trade?

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ABSTRACT

How Does Financial Inclusion Affect Firm Performance and Participation in Trade?

This paper extends on the work by Chauvet and Jacolin titled "Financial inclusion, bank concentration, and firm performance," which focused on the importance of financial inclusion on a firm's ability to improve on its sales performance. Financial inclusion is the availability or equality of opportunity to access credits provided by the financial service providers. It helps firms to secure financial services to run their businesses, including the production and innovation expenses that they need, so that they can improve on their sales. Production and innovation expenses are not something easy to access as it contains heavy cost for the firms for example, launching a new product would require lot of research and experiment which requires sufficient funding which is possible through external sources. In such cases, financial inclusion comes into the picture. Financial inclusion is a key to reducing poverty and boosting prosperity ("World bank"). This paper deals with the data from developing countries which brings us to the fact that if the firms have financial inclusion, it will lead to prosperity and reducing poverty in the country. The rationale behind this cause is leading more productivity would result in more employment and labor participation, which would bring prosperity and reduce poverty in the country. Any firm who expands would also bring wealth to the people of its country by giving them jobs and improving the lifestyle of the country.

In this paper, I use the latest data from the World Bank Enterprise Survey from 161977 firms in 79 countries from 2006-2019 to test whether the results from the earlier studies are still significant. I also expand on the findings by examining whether firms are also more likely to trade when they have better access to financial services. Economies with better developed financial sectors tends to have a comparative advantage in manufacturing industries (Beck,2002).

Access to finance brings an opportunity to have more resources in the firm, which will help in producing more goods and services. hence, the business would expand not only at the country level but internationally too. Therefore, financial inclusion leads to participation in trade.

My results suggest that people who have a facility of loan or overdraft leads to more productivity and growth whereas, the one with low productivity requires financial inclusion to sustain and then expand their business to lead to productivity, prosperity and reducing poverty in the country. Also, the results show that firms having loan/overdraft facility leads to more participation in trade which answers our second research question about the effect of financial inclusion on international trade. Therefore, the analysis states that financial inclusion in firms has a positive relationship between productivity and participation in trade.