COMPARING FINANCIAL SYSTEMS: A STRUCTURAL ANALYSIS†

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Abstract. This paper provides structural and non-structural tests that compare the characteristics of financial systems across countries. Analyzing European data, we test whether the countries with a larger share of market finance in total external finance have more efficient financial markets (relative to other financial intermediaries such as banks). The identification strategy relies on the observation at the industry-level of macro data (the share of market finance in total external finance) and micro data (the distribution firm sizes). Specifically, we argue that the share of market finance increases less with the industry average firm size in countries with relatively more efficient financial markets. We find that the UK channels a larger fraction of the financial flow to the firms through financial markets than continental Europe but this is explained by larger firms in the UK, not relatively more efficient markets.

Keywords. Financial structure, distribution of firm sizes, structural estimation, heterogenous firms, aggregation.

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