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Access to Finance, Product Innovation and Middle-Income Traps

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Highlights

- Interactions between access to finance, product innovation, and labor supply are studied in an OLG model
- Distribution of skills is endogenous
- Lack of access to finance has an adverse effect on innovation activity, directly and indirectly
- indirect effect operates through decision to invest in skills
- Multiple steady states may emerge if monitoring costs fall with number of successful projects
- One is a middle-income trap, with small labor force and low wages in innovation, and low growth
- Alleviating constraints on access to finance may help to escape from that trap.

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