Financial Development and Economic Growth: The Case for Eight Asian Countries

Dipendra Sinha
Joseph Macri

This paper looks at the relationship between financial development and economic development using time series data for the following eight Asian countries: India, Japan, Korea, Malaysia, Pakistan, Philippines, Sri Lanka and Thailand. First, we estimate augmented production functions where the growth rate of income is made a function of the growth rates of capital, labour (population is used as a proxy for labour) and a financial development variable. For each regression, we use one of the four financial development variables. Second, we conduct multivariate causality tests between the growth rate of income and the growth rates of the financial development variables. Both types of estimations are preceded by extensive unit root tests of the variables. The regression results show a positive and significant relationships between the income variables and financial variables for India, Malaysia, Pakistan and Sri Lanka but not for other countries. The multivariate causality tests show that two-way causality between the income and the financial variables for India and Malaysia. For Japan and Thailand, there is one-way causality from financial variables to income variables while for Korea, Pakistan and to some extent for Philippines. the causality flow is in the reverse direction. For Sri Lanka, there is no evidence of causality flowing in either direction.

Keywords: finance, growth. Causality
JEL Classification: C32, E51, O10

Correspondence:
Department of Economics
Macquarie University
Sydney, NSW 2109
AUSTRALIA
jmacri@efs.mq.edu.au