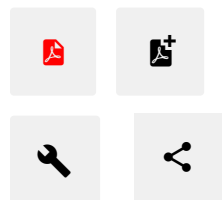




Financial Development and Economic Growth: International Evidence

Woo S. Jung



≡ More

Financial Development and Economic Growth: International Evidence*

Woo S. Jung
University of Kansas

I. Introduction

The importance of the relationship between financial development and economic growth has been well recognized and emphasized in the field of economic development.¹ Although recent writings on this subject seem to accept the hypothesis that financial development is crucial for successful economic growth,² Patrick asked the critical question, Which sector, financial or real, leads in the dynamic process of economic development?

Patrick identified two possible patterns in the causal relationship between financial development and economic growth. In the first, growth induces an expansion of the financial system.³ According to this

growth induces an expansion of the financial system. According to this view, called “demand-following,” the lack of financial growth is a manifestation of the lack of demand for financial services. As the real side of the economy develops, its demands for various new financial services materialize, and these are met rather passively from the financial side. In the second pattern the expansion of the financial system precedes the demand for its services. Channeling scarce resources from (small) savers to (large) investors according to relative rates of return, the financial sector precedes and induces real growth. The deliberate establishment and promotion of financial institutions in many less developed countries (LDCs) might reflect this belief in the “supply-leading” relationship between the two developments. A natural question then concerns the direction of causality between financial development and economic growth. Patrick asserted that the direction of causality changes over the course of development. In his view, financial development is able to induce real innovation-type investment before sustained modern economic growth gets under way, and, “as the process of real growth occurs, the supply-leading impetus gradually becomes less important, and the demand-following financial response

© 1986 by The University of Chicago. All rights reserved.
0013-0079/86/3402-0025\$01.00



THE UNIVERSITY OF CHICAGO PRESS JOURNALS

[The University of Chicago Press Books](#)

[Chicago Distribution Center](#)

[The University of Chicago](#)

[Accessibility](#)

[Open access at Chicago](#)

[Permissions](#)

[Statement of Publication Ethics](#)

[Diversity and Inclusion at the University of Chicago](#)

[Contact us](#)

[Terms and Conditions](#)

[Privacy Notice](#)

[Media and advertising requests](#)



