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Does banking sector development affect economic growth and inflation? A panel cointegration and causality approach

Rudra P. Pradhan , B. Mak Arvin, Neville R. Norman & Yasuyuki Nishigaki

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Abstract

Many studies investigate relationships between economic growth in specific economies and the development of its banking sector or between its growth rate and its rate of inflation. Advancing on earlier work, this article uses panel cointegration and causality tests applied to 34 OECD countries over the period 1960–2011. Our novel panel-data estimation procedure offers more robust estimates by utilizing variations between countries as well as variation over time. We identify important long-run causal links among the variables and show their implications for economic policy.

Keywords:

banking-sector development

economic growth

inflation

panel cointegration tests

panel Granger causality tests

OECD countries

JEL Classification:

O43

O16

E44

E31

Notes

- ¹ The large literature focusing on the various determinants of growth is not surveyed here. See, for example, Barro and Sala-i-Martin ([1995](#)), the May 1992 issue of the Economic Journal, and the various issues of the Journal of Economic Growth.
- ² See also FitzGerald ([2006](#)) for an excellent survey which also calls attention to the significance of the topic we study here. The author warns against seeking simple relationships and opines that many connotations of financial development may not be measurable.
- ³ Financial development may be interpreted as banking-sector development and/or stock market development. See, for example, Ang ([2008a](#)) for discussion.

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