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Nexus Between Financial Development and Economic Growth in Malaysia

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ABSTRACT
Financial development is the key for economy evolution as financial intermediaries could foster productivity growth and capital accumulation which lead to the economic growth. The nexus between financial and economic growth is an issue that has long been debated. On the one hand, a stream of literatures offer support to the contention on the running causality from financial development towards economic growth while on the other hand, economic variables are found to foster the financial institutions. Therefore, this study aims to investigate the relationship between financial development and economic growth in Malaysia over the period of 1990 to 2013. The research methods adopted are Johansen cointegration test to check the existence of short term and long term relationship between variables used and Granger causality test to determine the relationship direction for the different variables used. The study finds evidence of a long-run relationship between financial development and economic growth, amid a running causality between economic growth to all indicators of financial development in Malaysia with the exception of financial system deposit. The results imply economic growth can be further developed as it stimulates the development of financial indicators.
Keywords: Financial development, Economic Growth, Malaysia

INTRODUCTION
The economic growth of nations is largely dependent on a financial system which is largely built on stable financial development policies. In other words, financial development is the key for economy evolution as financial intermediaries could improve economic efficiency and growth by improving risk management, making financial transactions, savings mobility and make easy for the exchange of goods and services (Levine, 1997). Financial intermediaries could foster productivity growth (Beck et al., 2000; Ang, 2008) and capital accumulation which lead to the economic growth (King and Levine, 1993). This suggests that the efficiency of the financial system positively contribute to economic growth (Rachdi and Mbarek, 2011).