International Journal For Advanced Research In Science & Technology
A peer reviewed international journal
www.ijarst.in
ISSN: 2457-0362

EFFECT ON ECONOMIC GROWTH UNDER FINANCIAL INTERMEDIATION A REVIEW

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ABSTRACT

Cameroonian economic policy from 1988 restructured the financial sector towards a greater Financial Intermediation (FI). This article seeks to understand the influence of FI on economic growth in Cameroon. This principal objective is split into two specific objectives: (1) to determine the impact of FI on economic growth and (2) to identify the nature of the link between FI and Economic Growth in Cameroon. In order to attain this principal objective, we use secondary data for the period 1977 to 2006. The impact of FI on growth is realized by a multiple linear regression and the relationship between FI components and economic growth measured by GNP per capita is modeled by a Vector Auto Regression model. The study shows that FI has a positive and non-significant impact on economic growth in Cameroon through private credit, monetary mass, intermediation margin as well as bank restructuring. It also shows no causal effect of FI on growth and vice versa. This could be explained by the restructuring of the banking system, bank over liquidity, MFE's instability and poor growth environment. Thus banks and Micro Finance Establishments (MFE) might consolidate their management system in order to ensure their credibility as well as their continuity. The Banking Commission of Central Africa (COBAC) and the Cameroonian government should intensify the process of the stabilization of the micro finance sector and create a credible financial market.

INTRODUCTION

At the beginning of the 1960's, all the African countries beyond the political ideologies were confronted with the choice of development strategy. These development strategies (Planning and Structural Adjustment Plan) carried out under the impulse of the international institutions (World Bank, International Monetary Fund, African Development Bank) were based on the stimulation of the growth through investments, taking into account the financial component. After the fall of the oil prices and raw materials, the 1980s witnessed a massive debt of the developing countries. The Cameroonian economic policy since 1988 has restructured the financial sector towards a greater financial intermediation with the advent of structural adjustment and the promulgation of the 1990 and 1992 laws related to cooperative companies and common initiatives groups. Thus many cooperatives were created (MC2, MUFFA, Cofinest) in order to satisfy the marginalized population from classical banks. Taking into consideration the fact that, in any liberal economy, a well developed financial sector promotes economic activities, domestic investment and accumulation of wealth through credits and cost reduction of financial intermediation, we can say that Financial Intermediation (FI) has a special effect on Economic growth in Cameroon. Within this context, this article titled "Effect of Financial Intermediation (FI) on Economic growth in Cameroon" aims to determine the impact of the Financial Intermediation on Economic growth and to understand the nature of the link between FI and Economic Growth in Cameroun.

This is an activity through which an institutional unit acquires financial credit and simultaneously, contracts engagements on its own account by means of financial transactions on the market (Biales, 2006). Financial Intermediation has certain characteristics, among those, we can quote the three most important: (1) the fact that it is based on two bilateral relations: on one hand between the non-financial agent or the borrower and the financial intermediary and on the other hand between this intermediary and the source of financing used; (2) the fact that it supposes exchanges of information at the individual level whereas at the level of market information, it is collective and (3) the rate of intermediation which measures the share of the finances brought by the financial agents as a ratio of the finances from which the non-financial agents benefit. In a historitical way, we distinguish two types of intermediation; one in the broad sense and another in a strict sense. The first results from an approach known as the supply from financing because it gathers under the label of intermediate finances the whole of the contests granted to the non-financial agents by all the financial institutions. This rate calculated thus brings down the whole finances in which various institutions take part on the total of non-financial finances granted to agents. The second rate results from an approach known as the demand for financing because it privileges the choice that applicant made with the profit of recourse to financial intermediaries.

METHODOLOGY

On the basis of these hypotheses, we defined a certain number of variables justified on theoretical basis for each objective. The impact of FI on growth is achieved by a multiple linear regression model using secondary data for the period 1977 to 2006. We thus retained as endogenous variables representative of the concept of economic growth, the GDP per capita noted LGDP. Exogenous variables are logarithm of private credits (LCcmlt), logarithm of monetary mass (LM2), logarithm of Intermediation margin (LMi) and a dummy variable “D”. The Dummy represents banking reorganization taking value 0 before the reorganization and value 1 after banking reorganization in 1990.Then the relationship between FI components and economic growth is modeled by the Vector Auto Regression (VAR) model which captures the main problems of endogeneity and causality. Under the fundamental hypothesis that Financial Intermediation causes Economic growth, we define as endogenous variables representative of the concepts of economic growth and Financial Intermediation, the GDP per capita noted LGDP, LCcmlt, LM2 and LMi. Exogenous variables are constant variable and the lag variables. From our variables coded above, we obtain two models to be estimated as:

The multiple regression model :

LGDPt = B0 + B1 LCcmltt + B2 LM2t + B3 LMit + B4 Dt + et

With t= 1977…, 2006; n= 30 observations

B0; B1; B2; B3; B4 the model coefficients of regression assigned to the respective exogenous variables; Dt: the banking reorganization which is the Dummy variable.

The VAR model.

(LPib$t$LCcmlt$t$LM2t LMi)= (0 $a1$ $a2$ $a3$ $a4$ $b0$ $b1$ $b2$ $b3$ $b4c0$ $c1$ $c2$ $c3$ $c4$ $d0$ $d1$ $d2$ $d3$ $d4$)(1LPib$t-p$LCcmlt$t-p$LM2$t-p$ LMi$t-p$) +($\varepsilon1t\varepsilon2t\varepsilon3t$ $\varepsilon4t$)

With t=1977…, 2006; n= 30 observations; a0… 4; b0… 4; c0… 4; d0… 4 parameters of the model comparable to the coefficients of regression.

To model the relationship between private credits, monetary mass, financial intermediation margin and Economic growth, we use a multiple linear regression. Indeed, we use software Eviews7 to estimate the model. The model consists of an endogenous variable LGDP and four exogenous variables: LCcmlt; LM2, LMi and D the variable dummy representing the banking restructuration.

When time series data is used, it is first of all important that they preserve a constant distribution in time.With the help of the Dickey-Fuller Augmented test,

CONCLUSION

This article at the same time offers an empirical relativisation of the concept "intermediate market economy" and an illustration of the importance gained in recent years by the capital market. The econometric software Eviews enables us to carry out the different regressions. The test of Fischer made it possible to deduce that the first model of multiple linear regression is overall nonsignificant; but some exogenous variables in the model contribute to the explanation of economic growth. To this end the analysis of the signs of the coefficients enabled us to conclude that credits to private sector; monetary mass as well as intermediation margin induce in a positive way the growth. That confirms our first assumption. The Granger causality test of Toda-Yamamoto shows that Financial Intermediation does not have a causal effect on economic growth in Cameroon, contrary to several empirical studies which testify that it is FI that causes growth. This could be explained by unproductive investments (which are centered on the means and not the results), corruption and especially the diversions of funds in the attribution of government contracts which brings a bad quality of realization, or the period of study which would be very large and the effects are felt on the results. This disappearance is due to the fact that the socio-economic environments in which Banks and MFE as well as the amounts of the deposits and credits are differents. It should be noted that, Goldsmith in 1969, recognized that there is a link between the long run growth rate of the economy and the level of the evolution of financial sector.

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