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Authors: Muazu Ibrahim, Paul Alagidede

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Nonlinearities in Financial Development–Economic Growth Nexus: Evidence from sub-Saharan Africa

Nonlinearities in Financial Development–Economic Growth Nexus: Evidence from sub-Saharan Africa (SSA)*

Muazu Ibrahim*

School of Business and Law, Department of Banking and Finance

University for Development Studies

Post Office Box UPW 36, Wa, Upper West region

Ghana

Paul Alagidede

Wits Business School, University of the Witwatersrand

2 St. David's Place, Parktown, Johannesburg 2193

South Africa

*Corresponding author: imuazu@uds.edu.gh

Abstract

The impact of financial development on economic growth has received much attention in recent literature. However, there are potential discontinuities mediating finance–growth nexus that existing empirical studies have not rigorously examined. This study investigates whether the impact of finance on economic growth is conditioned on the initial levels of countries' income per capita, human capital and financial development for 29 sub-Saharan Africa countries over the period 1980–2014 using a sample splitting and threshold estimation technique. Our findings suggest that, while financial development is positively and significantly associated with economic growth, below a certain estimated threshold, finance is largely insensitive to growth while significantly influencing economic activity for countries above the thresholds. The main conclusion drawn is that higher level of finance is a necessary condition in long run growth and so are the overall level of income and human capital.

Keywords: Financial development; economic growth; threshold

JEL Classification: F4; F31; F32; C1

1.0 Introduction

The importance of financial development to economic growth has been given much credence in the literature. Indeed, early writers on this relationship have used financial systems in the

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