



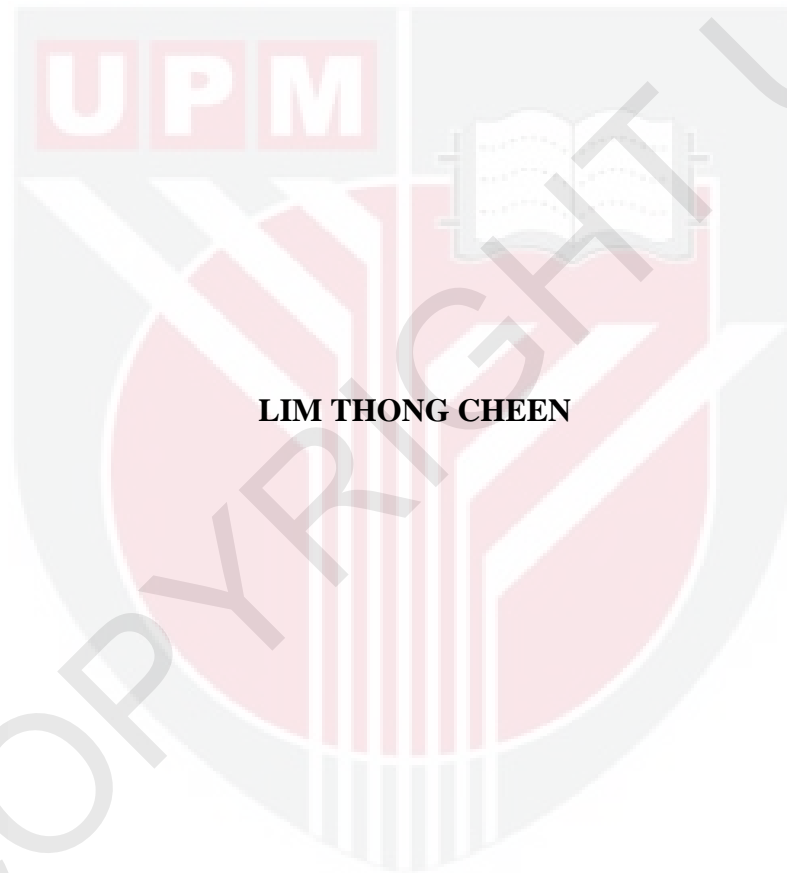
UNIVERSITI PUTRA MALAYSIA

***IMPACT OF SELECTED INSTITUTIONAL FACTORS ON ECONOMIC
GROWTH***

LIM THONG CHEEN

FEP 2011 21

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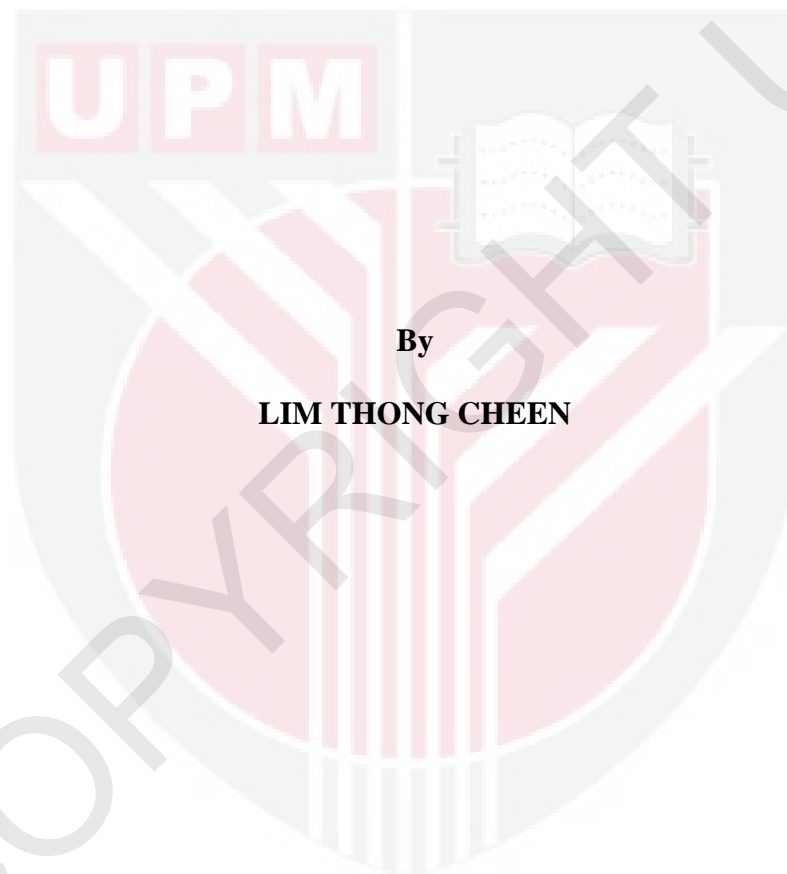


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**MASTER OF SCIENCE
UNIVERSITI PUTRA MALAYSIA**

2011

**IMPACT OF SELECTED INSTITUTIONAL FACTORS ON ECONOMIC
GROWTH**



By

LIM THONG CHEEN

**Thesis Submitted to the School of Graduate Studies, Universiti Putra Malaysia,
in Fulfilment of the Requirement for the Degree of Master of Science**

January 2011

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in fulfilment of the requirement for the degree of Master of Science

IMPACT OF SELECTED INSTITUTIONAL FACTORS ON ECONOMIC GROWTH

By

LIM THONG CHEEN

January 2011

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Faculty: Economics and Management

This study examines the relationship between institutions and economic growth at various stages of economic development. The specific objectives of the study are (1) to investigate the impact of institutions on economic growth, (2) to examine the causality effect between institutions and economic growth. The dataset consists of 60 countries, which is further divided into four stages, namely low-income, lower-middle income, upper-middle income and high-income countries. The institutions dataset is obtained from International Country Risk Guide (ICRG) covering the period 1990 to 2006.

The empirical results demonstrate that institutions have a significant impact on economic growth in the long-run in countries at various economic development levels except high-income countries. The results indicate that institutions (average) have positive significant impact on economic growth in lower-middle income and upper-middle income countries. However, not all the dimensions of institutions have equal explanatory capacity. Corruption and bureaucracy quality matter for economic growth

in low-income countries, whereas law and order have positive significant impact on economic growth in upper-middle income countries.

Besides, the panel Granger causality results also show that there is a bi-directional causality between institutions and economic growth. Institutions are more responsive in upper-middle income countries with respect to the causal effect. Among various institutions indicators, corruption is the most important institutions indicator that has Granger causality effect with economic growth. The findings also suggest that the causality patterns between institutions and growth vary at different stages of economic development levels. As a conclusion, institutions matter for economic growth and they have different directional causality effects, but the difference is according to the different level of economic development.

In terms of policy implications, this study suggests that governments or policy makers seeking to promote economic growth should focus on institutional reforms especially in lower-middle income and upper-middle income countries. Reducing corruption and improving bureaucratic quality are key factors to promote economic growth in low-income countries, while enhancing law and order is important to achieve higher economic growth for upper-middle income countries.

With respect to the causality effect, the low-income and lower-middle income countries should focus on country's economic growth and then higher economic development will further promote better institutions. On the other hand, the upper-middle income countries should concentrate on institutions in order to achieve greater economic growth. In addition, corruption is an important institutions indicator that

must be controlled in order to enhance higher economic growth for all groups of countries.



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Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi keperluan untuk ijazah Master Sains

KESAN FAKTOR INSTITUSI TERPILIH TERHADAP PERTUMBUHAN EKONOMI

Oleh

LIM THONG CHEEN

Januari 2011

Pengerusi: Profesor Madya Law Siong Hook, PhD

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Kajian ini bertujuan untuk menentukan hubungan antara institusi dan pertumbuhan ekonomi bagi negara pembangunan ekonomi yang berbeza. Objektif khusus kajian ini adalah (1) untuk menyiasat kesan institusi terhadap pertumbuhan ekonomi, (2) untuk menguji hubungan sebab akibat antara institusi dan pertumbuhan ekonomi. Kumpulan data ini terdiri daripada 60 buah negara, selanjutnya dibahagikan kepada empat tahap iaitu negara berpendapatan rendah, negara berpendapatan sederhana rendah, negara berpendapatan sederhana tinggi dan negara berpendapatan tinggi. Kumpulan data institusi diperolehi dari *International Country Risk Guide (ICRG)* bermula dari tahun 1990 hingga 2006.

Keputusan empirik menunjukkan bahawa institusi mempunyai kesan yang signifikan terhadap pertumbuhan ekonomi jangka panjang bagi pelbagai tingkat negara pembangunan ekonomi kecuali negara berpendapatan tinggi. Keputusan melaporkan bahawa institusi (purata) memberi impak positif signifikan terhadap pertumbuhan ekonomi di negara berpendapatan sederhana rendah dan negara berpendapatan sederhana tinggi. Namun, tidak semua dimensi institusi jelas mempunyai kapasiti

yang sama. Rasuah dan kualiti birokrasi adalah penting bagi pertumbuhan ekonomi di negara berpendapatan rendah, tetapi undang-undang dan ketenteraman mempunyai kesan positif terhadap pertumbuhan ekonomi di negara berpendapatan sederhana tinggi.

Selain itu, keputusan panel hubungan sebab akibat Granger menunjukkan bahawa wujudnya hubungan sebab akibat dua arah antara institusi dan pertumbuhan ekonomi. Institusi lebih responsif di negara berpendapatan sederhana tinggi berhubung dengan kesan hubungan sebab akibat. Di antara piawai institusi, rasuah merupakan piawai institusi paling berpengaruh kepada pertumbuhan ekonomi kerana wujudnya kesan hubungan sebab akibat Granger. Penemuan ini juga menunjukkan bahawa kesan hubungan sebab akibat untuk institusi dan pertumbuhan ekonomi berubah mengikut tahap pembangunan ekonomi yang berbeza. Secara kesimpulan, institusi adalah penting bagi pertumbuhan ekonomi and mempunyai kesan hubungan sebab akibat, tetapi berbeza mengikut tahap pembangunan ekonomi yang berbeza.

Dari sudut implikasi dasar, kajian ini mencadangkan kerajaan atau penggubal dasar yang berusaha untuk meningkatkan pertumbuhan ekonomi perlu memfokuskan reformasi institusi terutamanya di negara berpendapatan sederhana rendah dan negara berpendapatan sederhana tinggi. Membanteras rasuah dan meningkatkan kualiti birokrasi merupakan faktor penting untuk mendorong pertumbuhan ekonomi di negara berpendapatan rendah, sementara meningkatkan undang-undang dan ketenteraman juga penting untuk mencapai pertumbuhan ekonomi yang lebih tinggi untuk negara berpendapatan sederhana tinggi.

Sehubungan dengan kesan hubungan sebab akibat, negara berpendapatan rendah dan negara berpendapatan sederhana rendah haruslah fokus kepada pertumbuhan ekonomi di negara masing-masing dan peningkatan pembangunan ekonomi ini kemudiannya akan mempromosikan institusi yang lebih baik. Sebaliknya, negara berpendapatan sederhana tinggi haruslah fokus kepada institusi supaya mencapai pertumbuhan ekonomi yang lebih besar. Keputusan juga menunjukkan rasuah merupakan piawai institusi terpenting dan harus dikawal supaya membolehkan peningkatan pertumbuhan ekonomi yang tinggi bagi semua kumpulan negara.



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The contribution of them had helped me make this thesis possible. Thank you to all your readiness to help and support for me.

I certify that a Thesis Examination Committee has met on 6 January 2011 to conduct the final examination of Lim Thong Cheen on his thesis entitled “Impact of Selected Institutional Factors on Economic Growth” in accordance with the Universities and University College Act 1971 and the Constitution of the Universiti Putra Malaysia [P.U.(A) 106] 15 March 1998. The Committee recommends that the student be awarded the Master of Science.

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DECLARATION

I declare that the thesis is my original work except for quotations and citations which have been duly acknowledged. I also declare that it has not been previously, and is not concurrently, submitted for any other degree at Universiti Putra Malaysia or at any other institution.

LIM THONG CHEEN

Date: 6 January 2011

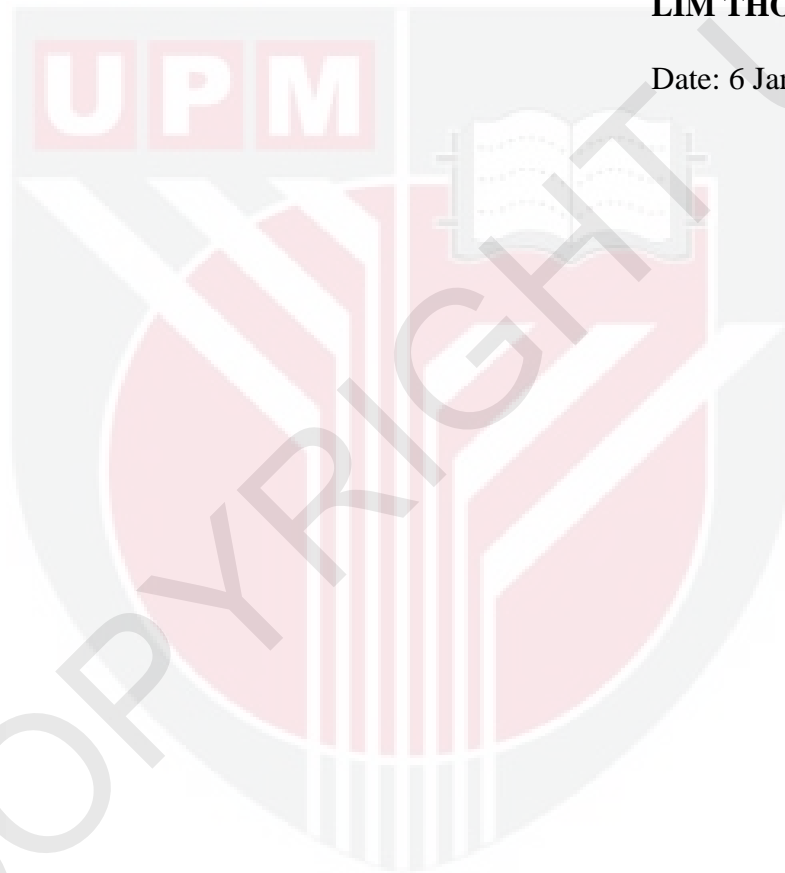


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