FINANCIAL INTEGRATION AND ECONOMIC GROWTH IN THE SOUTHERN AFRICAN DEVELOPMENT COMMUNITY

Ch. Paramaiah, Skyline University College
Sello M.N. Lesotho Revenue Authority Lesotho
Pranav Kumar, Skyline University Machema R, National University of Lesotho

ABSTRACT

In this paper, an attempt has been made to assess the relationship between financial integration and economic growth in the Southern African Development Community (SADC). The nexus between financial integration and economic growth works through several channels such as enabling the flow of funds across countries. This flow of funds augments the pool of available domestic savings. The financial integration is able to spur economic growth, therefore, several countries have adopted financial integration agendas in order to boost growth. The empirical evidence on the effects of financial integration on economic growth is not conclusive. In this paper, a modest attempt has been made to investigate relationship financial integration and economic growth in the SADC region. This study employed the Chin-Ito index and the ratio of Foreign Direct Investment (FDI) to Gross Domestic Product (GDP) to measure financial integration in the SADC region. The results reveal that there is a positive and statistically significant relationship between financial integration and economic growth in the SADC countries. The findings, therefore, underscore the need for SADC to engage in policies that would position SADC as the preferred destination for FDI.

INTRODUCTION

Deciphering the causes of economic growth has for ages been one of the central issues in macroeconomics. Among the many scholars that have weighed in on causes of economic growth is Solow (1956), who proposed that economic growth is caused by savings. According to Solow (1956) the growth-augmenting effect of savings depends on the ability of savings to result in a corresponding increase in investment which eventually leads to economic growth and development. Thus, one of the implications of Solow (1956)'s proposition is that economic growth can be achieved by increasing the savings rate. This is because capital mobility allows consumption-smoothing, reducing risk, and stimulates investment and hence economic growth beyond the limits of domestic savings.

Prasad et al. (2007) also notes that capital flows boost a country's growth and by extension alleviates poverty by augmenting domestic savings, reducing the cost of capital, increasing productivity through transferring technological knowledge, and stimulating the domestic financial sector development. Because of the positive effect of capital flows on economic growth alluded to above that financial integration has increased worldwide. Specifically, this integration has been due to the increased globalisation of investments in search of better returns and risk diversification opportunities. In addition, most countries have endeavoured to entice capital inflows by liberalising restrictions on capital flows as well as deregulating financial markets (Agenor, 2003).