

DETERMINANTS OF ECONOMIC GROWTH IN MALAYSIA 1970-2010

By

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ABSTRACT

Economic growth of a country can be seen in term of increase or growth of Gross Domestic Product (GDP). The rapid economic growth will result in per capita income growth and changes in national economic sectors. Thus economic growth is an important indicator in measuring economic development. The objective of this study is to examine the determinants of economic growth in Malaysia. This study uses trade openness, foreign direct investment, government development expenditure and gross fixed capital formation as an independent variables. The empirical analysis is based on time series data for 40 years for period 1970 to 2010. The model that used to tested the long run relationship is by using Johansen and Juselius cointegration approach shows that trade openness, foreign direct investment, government development expenditure and gross fixed capital formation are the determinants of economic growth in a long run. On the other hand, results that based on Vector Error Correction Model (VECM) shows that trade openness and foreign direct investment are the significant determinants of economic growth in a short run but bring negative impact to economic growth. Furthermore, an ECM variable is negative and significant, that postulates the cointegration among given variables. The response coefficient value is -0.343895 , that suggesting moderate adjustment behavior, approx 34.4% percent of the disequilibria of the previous period's shock adjust back to the long run equilibrium in the current year. Based on causality test in this study found that, firstly OPEN variable is Granger cause to GDP variable. Secondly is GDP variable is Granger cause to GDE variable. Thirdly is GDP variable is Granger cause to GFCF variable. Fourthly is OPEN variable is Granger cause to FDI, GDE and GFCF variables. Based on the Ordinary Least Squares (OLS) regression in this study shows that trade openness, government development expenditure and gross fixed capital formation fixed at 1 per cent significance level. This indicates that these variables have a positive effect on economic growth in Malaysia. While foreign direct investment variable is not significant to the growth of Malaysian economy. Results also shows that government development expenditure is the highest variables affect Malaysia economic growth of 1% increase in development expenses will lead to the growth rate increase by 2.16%. Second highest variable is trade openness of a 1% increase in trade openness will lead to 1.28% increase in the growth of the Malaysian economy. Third highest variable is gross fixed capital formation of a 1% increase in gross fixed capital formation will lead 0.98% increase in economic growth in Malaysia. Results obtained in this study suggest that policymakers should keep an eye on all of the significant variables since it will give impact on economic growth.

ABSTRAK

Pertumbuhan ekonomi sesebuah negara boleh dilihat dari sudut peningkatan atau pertumbuhan keluaran Negara kasar (KDNK). Pertumbuhan ekonomi yang pesat akan menghasilkan pertumbuhan pendapatan perkapita dan perubahan besar dalam sektor ekonomi negara. Kajian ini mempunyai objektif untuk mengkaji faktor-faktor penentu pertumbuhan ekonomi di Malaysia. Kajian ini menggunakan keterbukaan ekonomi, pelaburan langsung asing, perbelanjaan pembangunan kerajaan dan pembentukan modal tetap kasar sebagai pembolehubah bebas. Analisis kajian ini adalah untuk tempoh 40 tahun bermula tahun 1970 sehingga tahun 2010. Ujian kointegrasi berdasarkan pendekatan Johansen dan Juselius menunjukkan bahawa keterbukaan ekonomi, pelaburan langsung asing, perbelanjaan pembangunan kerajaan dan pembentukan modal tetap kasar sebagai penentu kepada pertumbuhan ekonomi dalam jangka masa panjang. Keputusan berdasarkan Model Pembetulan Ralat (VECM) bagi hubungan jangka pendek menunjukkan keterbukaan ekonomi dan pelaburan langsung asing signifikan terhadap pertumbuhan ekonomi dalam jangka masa pendek tetapi memberi kesan negatif kepada pertumbuhan ekonomi. Tambahan pula, pembolehubah ECM adalah negatif dan signifikan. Pembolehubah ini menunjukkan lebih daripada 34.4 % pelarasan jangka pendek bagi penentu pertumbuhan ekonomi Malaysia. Hasil penganggaran '*Ordinary Least Squares*' (OLS) yang diuji dalam kajian ini menunjukkan bahawa keterbukaan ekonomi, perbelanjaan pembangunan kerajaan dan pembentukan modal tetap kasar pegun pada aras keertian 1 peratus. Ini menunjukkan bahawa pembolehubah ini memberi kesan positif kepada pertumbuhan ekonomi Malaysia. Manakala pembolehubah pelaburan langsung asing adalah tidak signifikan terhadap pertumbuhan ekonomi Malaysia. Hasil penganggaran ini menunjukkan bahawa perbelanjaan pembangunan kerajaan adalah pembolehubah yang paling tinggi memberi kesan kepada pertumbuhan ekonomi Malaysia iaitu 1% peningkatan dalam perbelanjaan pembangunan akan menyebabkan 2.16% peningkatan dalam pertumbuhan ekonomi Malaysia. Pembolehubah kedua tertinggi ialah keterbukaan ekonomi iaitu 1% peningkatan dalam keterbukaan ekonomi akan menyebabkan 1.28% peningkatan dalam pertumbuhan ekonomi Malaysia. Pembolehubah ketiga tertinggi ialah pembentukan modal tetap kasar iaitu 1% peningkatan dalam pembentukan modal tetap kasar akan menyebabkan 0.98% peningkatan dalam pertumbuhan ekonomi Malaysia. Hasil kajian menjadi satu petunjuk bahawa pembuat polisi seharusnya lebih peka kepada pembolehubah-pembolehubah yang signifikan ini semasa menggubal polisi kerana ianya merupakan faktor penting yang mempengaruhi pertumbuhan ekonomi.

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ABBREVIATIONS

ADF	--- Augmented Dicky Fuller
AIC	--- Akaike Information Criterion
ARCH	--- Aauto-Regressive Conditional Heteroskedasticity
D-8	--- Developing Eight Organization
ECM	--- Error Correction Model
FDI	--- Foreign Direct Investment
GCC	--- Gulf Cooperation Council
GDP	--- Gross Domestic Product
GFCF	--- Gross fixed capital formation
IMF	--- International monetary fund
INC	--- Per Capita Income
INF	--- Inflation
LDC	--- Less Developed Country
LM	--- Lagrange Multiplier
MWALD	--- Modified Wald Test
NKRA	--- National Key Result Area
NEP	--- New Economic Policy
OLS	--- Ordinary Least Square
OPEN	--- Trade openness
R&D	--- Research and Development
SAARC	--- South Asian Association for Regional Cooperation
VAR	--- Vector Autoregressive
VECM	--- Vector Error Correction Model

CHAPTER ONE

INTRODUCTION

1.1 Introduction

Sustainable economic growth is a desire of every countries in the world. Malaysia continue to move towards its vision of becoming a high-income developed country. Sustainable economic growth is an important factor to a country because a country can provide a good living standard for community (Osman, 1994). Malaysia is a country that practices a system of export oriented open economy. Malaysia economic growth is measured based on the percent change in the rate of Gross National product (GDP). When a country GDP increased from the previous year, the country is said to have growth in economy. The growth rate is equal to the percentage change in real GDP.

Lai (2003) state that economic growth is one of the key performance measures in the development and growth of the national economy. Economic growth shows the development of physical economy as an additional infrastructure and infrastructure increased from time to time and also will improve the living standards of the people as real income increases from time to time. Chaudhari (1989) defines the gross domestic product (GDP) as the total market value of all goods and services produced within the borders of a country for a period of one year. Lai (2002) also defines GDP as the total value of final goods and services produced by the factors of production owned by locals and foreign national of country.

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