How does the finance-growth nexus change with respect to:
  - inflation,
  - government size,
  - trade openness,
  - per capita income?

The results suggest that
  - high inflation crowds out positive effects of financial depth on growth
  - small government sizes hurt low-income countries
  - large government sizes hurt high-income countries
  - low levels of trade openness are sufficient in high-income countries
  - low-income countries need higher levels of trade openness
  - catch-up effects are higher for moderate per capita income levels.
Data and Estimation Methodology

Data

- World Development Indicators
- 5-year data for 84 countries between 1965–2004
- real per capita GDP growth
- log initial per capita GDP
- log initial secondary enrollment rate (SEC)
- the ratio of liquid liabilities (i.e., M3) to GDP
- the ratio of M3 less M1 to GDP
- inflation rate
- openness
- government size.

Estimation Methodology

- two-stage least squares with initial values as instruments
- time fixed effects for the 5-year periods
- rolling-window regressions with a constant window size of 120 after ordering the data according to the threshold variable (e.g., inflation).
Estimation Results

- Inflation and the finance-growth nexus:

- Government size and the finance-growth nexus:
Estimation Results

- We have positive effects of finance on growth when:
  - inflation rate is below 8 percent
  - government size (% GDP) is between 11 and 19 percent
  - trade openness (% GDP) is between 35 and 75 percent
  - per capita income level is above $665

- Financial-depth effects on growth have decreased over time