Chapter 6
Model and Model-Driven Methodology

ABSTRACT
This chapter specifies the empirical model used in the study, which is a Kaleckian post-Keynesian model, as an alternative to mainstream neoclassical theory. Having discussed the theory of financial intermediation in chapter two and commonality between post-Keynesian models of growth and endogenous growth theory in chapter three, this chapter postulates that financial development influences economic growth through different channels including investment, savings, and productivity growth. Later in the chapter, data characteristics, including stationarity, cointegration, and causality are reviewed. The chapter closes with a discussion about the main econometric modelling implemented in this research, including structural autoregressive modelling, impulse response analysis, and the variance decomposition method.

6.1 INTRODUCTION
The purpose of this chapter is to present the empirical foundations of a relatively recently developed Post-Keynesian theoretical framework. This model is built around theoretical discussion provided in chapter Two and Three. The orientation of financial sector development has given rise to question of “How does financial
development promote economic growth and development?” which has attracted attention from Modern Growth theorists. The main concern in this chapter is to discuss the empirical model derived from the theoretical model presented in the previous chapter, and to investigate the empirical question of “does financial development promote economic growth and development?” Given the main arguments in the previous chapter, one can see a Kaleckian-Post Keynesian emergence as an alternative to main stream neoclassical theory. This paradigm that assumes the past is unalterable and the future is uncertain, can relate investment, employment, income distribution and economic growth explicitly and short- and long-run analysis can be distinguished. Therefore in this chapter, a particular Kaleckian-Post-Keynesian macroeconomic model is theoretically and empirically explored.

Putting forward the endogenous growth theory of financial intermediation in Chapter Two and commonality between Post-Keynesian models of growth and endogenous growth theory in Chapter Three, this chapter posits that financial development may affect economic growth through three channels: investment, savings and productivity growth, using three different and conventional measures of financial development for selected East Asian countries. In terms of econometric approaches, the effect of financial development on key macroeconomic indicators is tested using time series regression and structural VAR modelling. This chapter also discusses the econometric method and various data issues.

This chapter develops as follows: Section 2 discusses our selected Kaleckian Post-Keynesian model of economic growth in detail and justifies the inclusion of equations into this model. Section 3 presents the empirical model including the financialisation of the model that is the exogenous inclusion of financial development variables into different equations of the model. This is in line with the theory of financial intermediation and is the main contribution of this research. The final econometric model will be presented at the end of this section. Section 4 reviews the estimation techniques of pre-analysis; including data characteristics in terms of stationarity, cointegration and Granger causality analysis. Section 5 reviews the main estimation techniques adopted in this research including Vector Auto Regressive (VAR) and Structural VAR, along with impulse response analysis and Variance decomposition techniques.

6.2 THE THEORETICAL MODEL

The model presented here is a Post-Keynesian open economy model, which is an extended version of Bhaduri and Marglin (1990). It consists of behavioural functions for investments, saving, and international trade defining the goods market and the
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