UNIVERSITI TEKNOLOGI MARA

THE RELATIONSHIP BETWEEN FINANCIAL DERIVATIVES AND ECONOMIC GROWTH: A STUDY ON ASIAN COUNTRIES

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ABSTRACT

There is immense and sturdy evidence that financial sector development affects economic growth for various samples across countries or regions. However, most of the studies researched the impact of the banking and stock market financing on economic growth. Less attention has been paid to links between financial derivatives and economic growth. Thus, this paper aims to explores the relationship between the financial derivatives and the economic growth of Asian countries. This study relies on the relationship between the independent variable, namely commodity futures, stock index futures, domestic credit to private sector, inflation (consumer price index), real interest rate, and trade openness, and the dependent variable of economic growth, proxy by GDP per capita growth, in four Asian countries for the period of 2011 until 2020. The relationship between each independent variable on the dependent variables, has been tested using a multiple regression model. The result of this study shows that in the selected four Asian countries, the stock index futures, inflation (consumer price index), and trade openness have a significant relationship with the economic growth. This result is in line with a study done by Sendeniz-Yuncu et al. (2007) and Vo et al. (2019), as both studies found out that these three variables have a significant relationship with GDP. In addition, this paper concludes with several recommendations for policy- and decision-makers that may help promote the use of derivatives markets to boost economic growth together with some recommendations for future studies.

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TABLE OF CONTENTS

	Page
AUTHOR'S DECLARATION	**ii**
ABSTRACT	**iv**
ACKNOWLEDGEMENT	**v**
TABLE OF CONTENTS	**vi**
LIST OF TABLES	**viii**
LIST OF FIGURES	**ix**
LIST OF SYMBOLS	**x**
LIST OF ABBREVIATIONS	**xi**
CHAPTER ONE INTRODUCTION	**1**
1.1 Introduction	1
1.2 Research Background	2
1.3 Problem Statement	2
1.4 Research Questions	3
1.5 Research Objectives	3
1.6 Significance of the Study	4
1.7 Scope of the Study	5
1.8 Limitation of the Study	5
1.9 Definition of Key Terms	5
1.10 Summary	7
CHAPTER TWO LITERATURE REVIEW	**9**
2.1 Introduction	9
2.2 Financial Derivatives and Economic Growth	9
2.3 Commodity Futures	10
2.4 Stock Index Futures	11
2.5 Domestic Credit to Private Sector	11
2.6 Inflation, Consumer Price Index	11
2.7 Real Interest Rate	12

CHAPTER ONE
INTRODUCTION

1.1 Introduction

Financial derivative is a monetary tool that derives its value from an underlying asset including stock, commodity, currency, index, bond, and equity. The common derivatives are future, forward, swap, and options. Nowadays, financial derivatives market is the largest segment of the financial market (Oliinyk, Burdenko, Volynets & Yatsenko, 2019), where it is one of the alternatives taken by many countries to reduce market risks and boost the economic growth of the country.

Furthermore, businesses use derivatives to hedge risks and minimize uncertainty about future prices (Abuselidze, Reznik, Slobodianyk & Prokhorova, 2020). The development of the economic growth relates to the need of priority usage of derivatives to accumulate financial resources on the world capital market, where it transfers, hedge and insure against risk. Financial derivatives play a vital role in a financial system and greatly contributes to the economic growth (Vo, Huynh, Vo & Ha, 2019). The rapid development of financial derivatives has led many researchers to study the relationship between the derivatives market and economic growth.

Developed economies are heavily counting on their financial markets. Growth of financial market has positive impact on the economic growth. Financial markets of developed economies are using derivative tools to minimize the risk of market participants (Perveen, Ahmed & Begum, 2018). The rapid development of the derivatives market has prompted researchers to study the relation between the derivatives market and economic growth (Oliinyk et al., 2019).

Derivatives markets are populated by four main types of contracts, namely forwards, futures, options, and swaps. The general concepts are similar, with their value derived from the price of an underlying asset. Focusing on six independent variables namely commodity futures, stock index futures, domestic credit to private sector, inflation (consumer price index), real interest rate, and trade openness, this study aimed to study the relationship between the financial derivatives and the economic growth of Asian countries.