

The Nexus between Growth and Saving :

Determinant of Gross Domestic Savings in Developing Countries : The Case of Ethiopia

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The general objective of this thesis is to investigate the long run and short run determinants of gross domestic saving and to examine the direction of causalities between economic growth and gross domestic saving in Ethiopia, using a time series annual data from the year 1975 to 2014. To investigate the causal relationship between economic growth and gross domestic saving in Ethiopia, the study has been employed the Toda-Yamamoto and Dolado- Lütkepohl (TYDL) approach to Granger non-causality test. The TYDL approach uses the Modified Wald Test (MWALD) to avoid the problems related to the non-standard asymptotic properties of non- stationary variables.

The estimation results of the study shows us that, there is bidirectional (feedback) causality between economic growth and gross domestic saving in Ethiopia. This implies that, the past values of gross domestic saving have a predictive ability in determining the current values of economic growth, and the reverse is also true. Indeed, the co-integration and Vector Error Correction Model (VECM) approach have been utilized to investigate both the long-run and short-run determinants of gross domestic saving in Ethiopia. Results from Augmented Dickey-Fuller and Phillips-Perron tests indicate that, all the variables of consideration are integrated of the same order, which are, $I(1)$. And results from the Johansen test of co-integration show us that, there is a long-run relationship among the gross domestic saving and the rest of all the explanatory variables.

As determinants of the gross domestic saving, the long-run coefficients of real interest rate and the lagged values of gross domestic saving are positive and statistically significant at 1% level of significant, while the long-run coefficients of total consumption expenditure is negative but statistically significant at 1% level of significant. The long-run coefficients of gross disposable income is positive and statistically significant at 5 % level of significant. While, the long-run coefficients of the budget deficit, current account deficit, are negative, but statistically insignificant, the long-run coefficient of financial deepening is positive but statistically insignificant.

Based on the estimation results of the short-run dynamic modeling (VECM), the coefficient of the error correction term is 9.5%, which implies that, about 9.5% deviations from the long-run equilibrium will adjust every year. It takes more than 10 years for the model to be at its long-run equilibrium. In the short-run, the financial deepening, real interest rate and current account deficit are significant determinates of gross domestic saving at 5% significant level, while the total consumption expenditure and the lagged values of gross domestic saving are significant detriments at 10% level of significant.