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**Law, Politics and Finance**

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## Abstract

Abstract of thesis entitled “Law, Politics and Finance” is submitted by Zhu Lin (M-B0-5634-8) for the degree of master of Social Sciences in Economics at the University of Macau in June 2012.

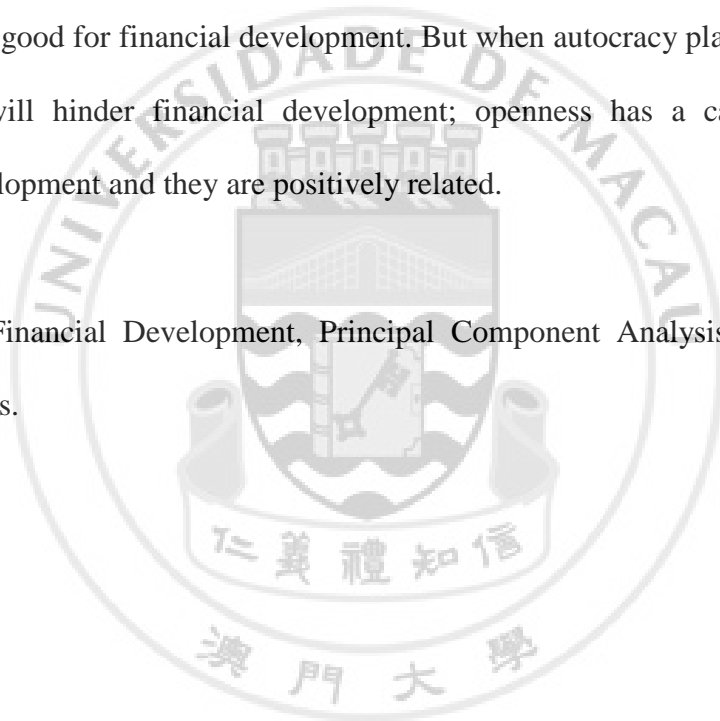
No two countries have the identical development degree in this world, taking into account of endowments, regulations, culture, and the national force.

The purpose of this paper is to study the determinants of financial development from the law and the politics aspects. Many economists are zealously working on the innovative view based on La Porta, Lopez-de-Silanes, Shleifer and Vishny (1996) (hereafter LLSV) “Law and the quality of its enforcement are potentially important determinants of what rights security holders have and how well these rights are protected.” I intend to examine empirically how law promotes financial development and whether politics can help to explain financial development taking the endowment factors into consideration. As in LLSV (1996), no socialist or “transition” economies are included in the sample. 49 countries are selected from Europe, North and South America, Africa, Asia and Australia. For consistency and the convenience of results’ comparison, I continue to use the same country sample. As this paper studies the impacts of law and politics on financial development through cross-country analysis, I assembled a typical data set covering legal origins, quality of legal enforcement, politics and other related macro-economic indicators in 49 countries ranging from 1990 to 2009. This paper adopts principal component analysis (PCA) to find out the proxy for financial development, which is a statistical method used to find out the

most informative proxies among a group of them.

Our analysis yields the following results: 1) the indicators measuring economic development explain the financial development well; inequality and inflation rate will make finance deteriorate. 2) The France or Spain legal origin countries don't have a high rate of financial development, while countries with German legal origin are the opposite. Still common law countries are good for financial development. As expected, institutional development and financial development are positively correlated. 3) Democracy is good for financial development. But when autocracy plays an important role, polity will hinder financial development; openness has a causal effect on financial development and they are positively related.

Key words: Financial Development, Principal Component Analysis (PCA), Legal Origin, Politics.



## Declaration

I declare that this thesis represents my own works, except where due acknowledgement is made, and that it has not been previously included in a thesis, dissertation or report submitted to this University or to any other institution for a degree, diploma or other qualification.

Signed \_\_\_\_\_



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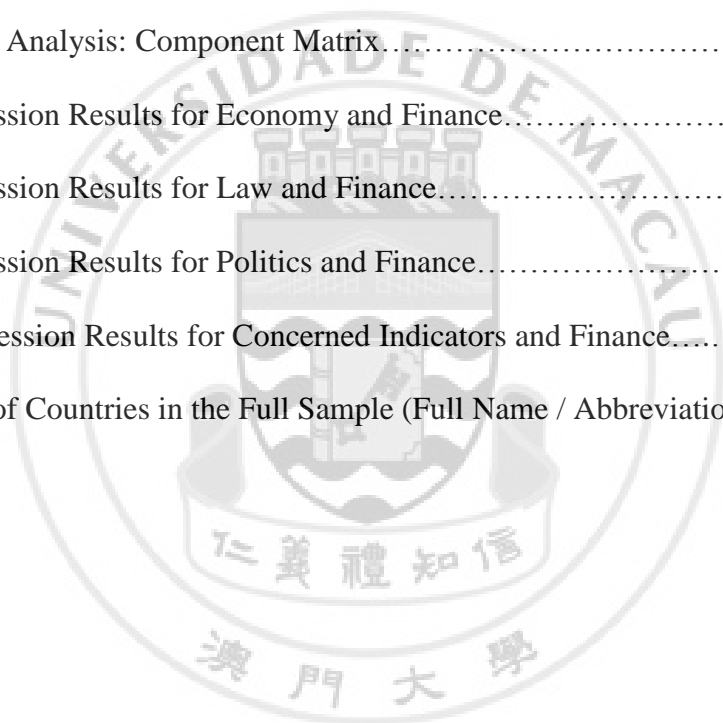


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## Notations

LLGDP	share of liquid liabilities to GDP
PCRDBOFGDP	ratio of private credit by deposit money banks and other financial institutions to GDP
OVERHEAD	share of overhead costs to bank's total assets
NETINTMARGIN	ratio of bank's net interest revenue to total earning assets
CONCENTRATION	share of assets of three largest banks to the assets of all commercial banks
STMKTCAP	ratio of value of listed shares to GDP
STVALTRADED	ratio of the value of total shares traded to average real market capitalization
STTURNOVER	ratio of the value of total shares traded to average real market capitalization
FRSP_MOM	the legal origin is French civil law
SCAN_MOM	the legal origin is Scandinavian civil law
GER_MOM	the legal origin is Germany civil law
UK_MOM	the legal origin is English common law
RULE_OF_LAW	reflects the efficiency of institutions
GINI	GINI coefficient
EDU	ratio of Person who completed primary, secondary and tertiary to population
INFLATION	inflation rate
LGDP	Log of Real gross domestic product per capita
DEMOCRACY	Qualities of democratic authority in governing institutions.
AUTOCRACY	Qualities of autocratic authority in governing institutions.
POLITY	democracy score minus autocracy score
OPENC	exports plus imports divided by GDP (the total trade as a percentage of GDP)