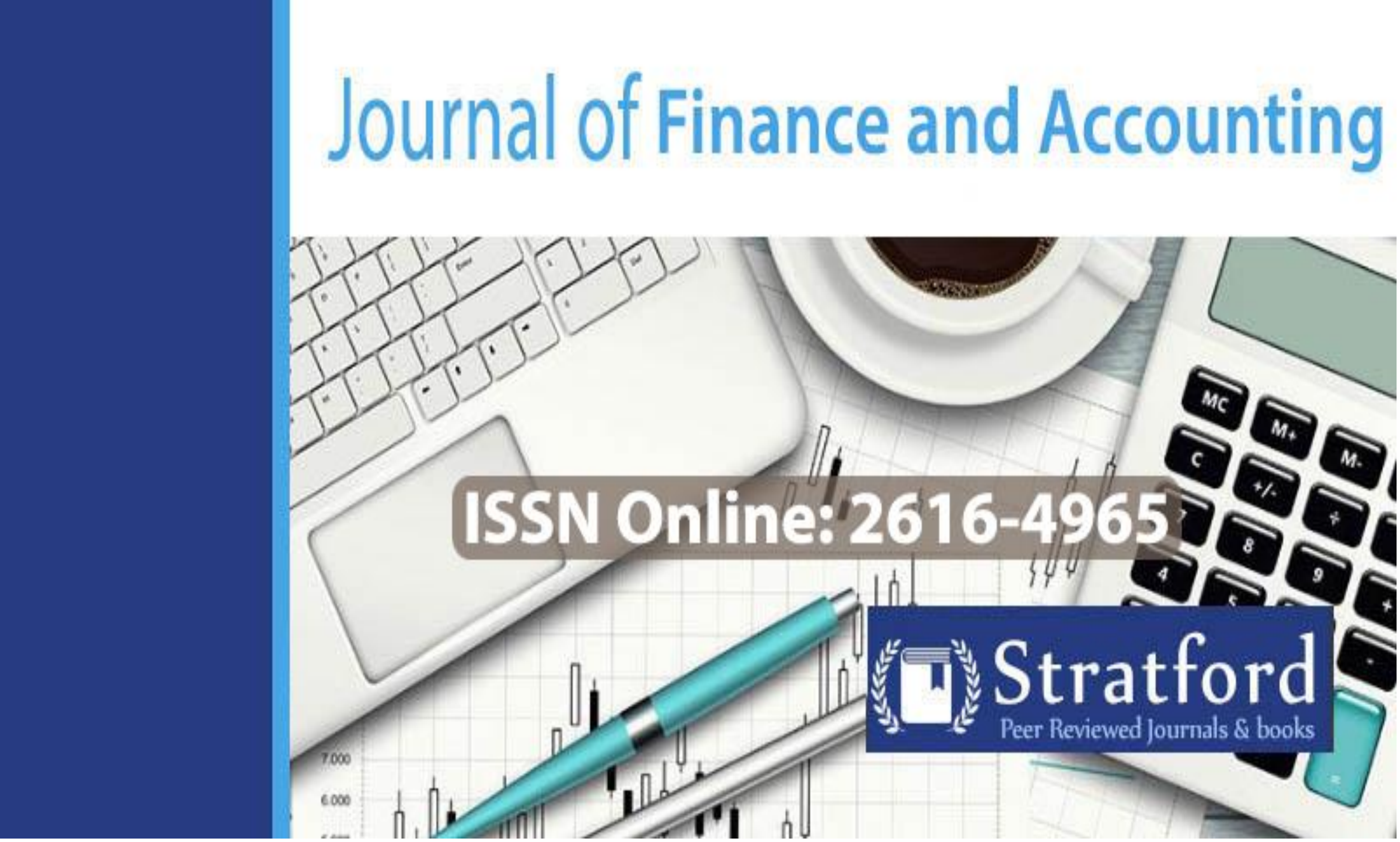

Financial Market Development and Economic Growth in Sweden

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ISSN: 2616-4965

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***How to cite this article*: Badwan, J. A., Thaver, P. J., & Hossin, J. F. (2023). Financial Market Development and Economic Growth in Sweden. *Journal of Finance & Accounting*, 7(9), 12-20. https://doi.org/10.53819/81018102t5269**

Abstract

Financial market development plays a crucial role in fostering economic growth by providing an efficient platform for the allocation of funds. As financial markets become more sophisticated and inclusive, they enable businesses to access capital more readily for investments in productive assets and innovative projects. Additionally, well-functioning financial markets encourage savings, promote risk-sharing, and enhance liquidity, facilitating economic expansion. Governments and policymakers play a pivotal role in nurturing financial market development through prudent regulations and incentives to drive economic growth and stability. Findings from studies on financial market development and economic growth in Sweden indicate a strong positive relationship between the two variables. Sweden's well-developed financial markets, characterized by a robust banking sector and capital markets, have been instrumental in promoting economic growth and stability. This is particularly evident in Sweden's ability to efficiently allocate capital, encourage innovation, and facilitate a high level of savings, contributing to its strong economic performance. In conclusion, the relationship between financial market development and economic growth in Sweden is robust and mutually reinforcing. Sweden's well-established financial markets, including a strong banking sector and capital markets, have been instrumental in driving the nation's sustained economic growth. These findings underscore the importance of nurturing financial market development as a vital component of fostering economic expansion and stability in Sweden. The study recommended that to further enhance the synergy between financial market development and economic growth in Sweden, policymakers should focus on maintaining regulatory stability and fostering innovation in the financial sector. Promoting financial inclusion to ensure that a broader section of the population can access and benefit from the opportunities offered by well-developed financial markets can be a valuable strategy for driving economic growth.

Keywords: *Financial Market Development, Economic Growth, Sweden*

Stratford Peer Reviewed Journals and Book Publishing
Journal of Finance and Accounting
Volume 7||Issue 9||Page 12-20||November||2023|
Email: info@stratfordjournals.org ISSN: 2616-4965

1.0 Introduction

The relationship between financial market development and economic growth has been a topic of significant interest among economists and policymakers. Sweden is a highly developed economy with a well-established financial sector, it is important to examine how the growth of financial markets contributes to overall economic prosperity. Streng and Örneblad (2021) mentioned that Sweden boasts a mature and sophisticated financial market, characterized by a well-functioning banking system, a highly active stock market, and a robust regulatory environment. Its financial system's development is reflected in the high level of financial intermediation, efficient allocation of capital, and strong investor protection (Eidestedt, Forsman & Unlu, 2020). The Swedish banking sector plays a vital role in financial market development. With a concentration of large and stable commercial banks, it facilitates access to credit for both businesses and individuals. These institutions also offer a wide range of financial services, contributing to economic growth by supporting investment, consumption, and risk management.

The Stockholm Stock Exchange (Nasdaq Stockholm) is the largest stock market in the Nordic region, making it a key player in the country's financial market development. The stock market acts as a platform for companies to raise capital, fostering entrepreneurship and innovation (Zeqiraj, Sohag & Soytas, 2020). It also enables individuals to invest in the market, encouraging savings and wealth accumulation. Sweden is known for its embrace of financial technology (FinTech) and innovation. The development of digital payment systems, online banking, and mobile financial services has increased financial inclusion, allowing a broader segment of the population to participate in the financial sector. These innovations contribute to overall economic growth by enhancing efficiency and convenience. Sweden has a strong regulatory framework and investor protection mechanisms. A well-regulated financial market builds trust and confidence among investors, both domestic and foreign, thereby encouraging capital inflows (Demekas & Nerlich, 2020). This enhances financial stability and supports long-term economic growth.

There is a positive correlation between financial market development and economic growth. As the financial sector expands, it becomes more efficient at allocating resources, leading to increased investment, productivity, and economic output (Asafo-Adjei, Boateng, Isshaq, Idun, Owusu Junior & Adam, 2021). Moreover, a well-functioning financial market can help smooth consumption, manage risk, and stimulate innovation. While financial market development is generally positive for economic growth, it also poses risks, such as financial instability, asset bubbles, and unequal wealth distribution. Therefore, it is essential to strike a balance between promoting financial development and ensuring stability. The Swedish central bank, Sveriges Riksbank, plays a critical role in maintaining financial stability and supporting economic growth. Its monetary policy decisions influence interest rates, inflation, and exchange rates, which, in turn, impact the financial markets and the broader economy (Inoue & Rossi, 2019).

Different sectors may be impacted differently by financial market development. For instance, the real estate and construction sectors may experience increased demand for loans due to lower interest rates, while technology companies may benefit from access to equity financing. Sweden's economic growth is also influenced by global economic conditions, including trade dynamics,

https://doi.org/10.53819/81018102t5269

international capital flows, and economic cycles. External factors can amplify or dampen the effects of domestic financial market development on the economy (Acheampong, 2019). Financial market development in Sweden is an integral part of the country's economic growth story. A well-developed financial sector, characterized by a strong banking system, a vibrant stock market, and technological innovations, has been instrumental in supporting entrepreneurship, investment, and economic development. However, the associated risks and challenges need to be carefully managed to maintain stability and ensure equitable growth. Sweden's financial market will continue to evolve, adapting to changing circumstances and global economic trends while contributing to the nation's continued prosperity (Torvanger, Maltais & Marginean, 2021). Understanding the dynamics of this relationship is essential for policymakers and stakeholders in Sweden's financial sector.

1.1 Statement of the Problem

The sustainability of Sweden's economic growth is a primary concern. As a developed nation, it faces the challenge of maintaining steady and robust growth rates. It is crucial to investigate whether the continued development of the financial market can contribute to sustainable economic growth or if diminishing returns may occur as the market matures. While financial market development is generally associated with economic growth, there is a risk of financial instability, as witnessed in the 2008 global financial crisis. Ensuring that the expansion of the financial sector does not lead to systemic risks and crises is a critical problem to address. Another problem area is the question of whether financial market development contributes to inclusive growth in Sweden. It is essential to examine if the benefits of a well-developed financial sector, such as increased investment and innovation, are distributed equitably across different socioeconomic groups or if they exacerbate income inequality.

The influence of financial market development on smaller enterprises, particularly startups and SMEs, is a matter of concern. It is necessary to investigate whether the growth of the financial sector in Sweden adequately caters to the financing needs of these businesses or if it primarily benefits larger corporations. The problem of regulatory and policy challenges emerges in the context of balancing the need for financial market development with the necessity of maintaining a stable and secure financial system. This problem requires an examination of the regulatory framework and potential adjustments to mitigate risks while fostering economic growth. Sweden's economy is closely intertwined with the global economy. The problem of how external factors, such as international economic conditions, trade dynamics, and global financial market trends, influence the relationship between financial market development and domestic economic growth is a critical area of study.

2.0 Literature Review

Siddik, Ahsan and Kabiraj (2019) noted that the 'MINT' quartet of countries; Mexico, Indonesia, Nigeria, and Turkey are expected to become major world powers by 2050. Leading it is anticipated that the financial development of these nations would be the driving force behind the actualization of the predicted result, as this has been asserted by authors and researchers in numerous studies.

Thus, the study examines the relationship between financial development and economic growth in the MINT over the 13-year period 2000–2012 by constructing a balanced panel dataset consisting of capital market activity variables such as market capitalization ratio to gross domestic product (GDP), number of listed securities, and value of transactions as ratios of GDP and gross fixed capital formation; with key explanatory variables. The study's findings indicate that the number of listed securities is the single most important indicator of capital market development for MINT economic growth. There was a negative and significant relationship between this indicator and GDP, but a positive and significant relationship between this indicator and the ratios of gross domestic savings and gross fixed capital formation to GDP. The growth of the capital market has a favorable impact on Indonesia, as measured by the rise in the country's gross domestic savings and gross fixed capital creation ratios. It is suggested that the duration of the research be extended so that long term econometric analysis may be performed.

Ekanayake and Thaver (2021) carried out study to examine the impact of financial sector development on the economic growth of 12 South American nations from 2010 to 2017 by employing a variety of financial sector variables. Three dynamic panel data models were estimated using a two-step system GMM approach; these models examine the impact of financial sector depth, access, and efficiency on economic development. The effect of financial sector development on economic growth is among the main debatable issue in economics and policymaking. This study proxied financial sector depth, access, and efficiency using the ratio of credit given to the private sector to GDP; the number of commercial bank branches per 100,000 adults; and the Return on assets. Accordingly, the findings showed that the breadth, accessibility, and efficiency of the financial sector positively affected the economic development of these nations. Increasing the availability of credit to the private sector is advised as a means of increasing the breadth of financial institutions. Further, financial institutions will need to take steps to improve their efficiency and broaden their reach in order to serve the public.

Raihan (2023) performed study to investigate the impact of financial market development on Economic growth using time series data in Uruguay. Many countries' financial markets have been undergoing adjustments for years or even decades. The actual ramifications of these changes, however, have been inconsistent. Three standard measures of monetary growth (broad money, deposit/GDP, and domestic lending to the private sector) were used in this analysis. Short-run positive relationships were found between monetary mass (M2), government expenditure, and economic growth when the Auto Regressive Distributive Lag (ARDL) method of estimation was used; short-run negative relationships were found between bank deposits, private investment, and economic growth. But all financial metrics reveal a good and considerable influence on economic growth in the long term. In this way, the bound test results show that all financial development indicators have a positive and lasting effect on economic growth. It is consequently advocated that the financial reforms in Uruguay should be pushed further in order to support the development of the financial market and therefore a rise in its effect on economic growth.

According to Pan and Mishra (2018), New Zealand's capital market performance and economic development were both boosted by the country's banks being recapitalized. However, recessions slowed economic growth and dampened stock market activity. Accordingly, this research used empirical facts to evaluate the impact of capital market performance on economic development in emerging nations from 2012 to 2022. The research set out to accomplish just that by looking at how different levels of market capitalization affect developing countries' actual GDP. For the conceptual, theoretical, and empirical basis of the research, relevant and related literature was evaluated. The research adopted a qualitative method utilizing descriptive synthesis to examine the findings of the influence of capital market performance on economic development in developing countries using empirical information from 2012 to 2022. 30% of empirical data from studies of capital markets and economic development in emerging countries were found to be inconsistent with the right expectation, according to the research. The research found that findings from time series analyses conducted in poor nations varied depending on the variables and methods used. The research concluded that domestic capital production in both capital and money markets should be encouraged to better fund businesses. Capital market studies need to harmonize their methods to get repeatable results.

Badwan (2022) conducted study to critically analyze the impact of financial markets and the magnitude and direction of economic growth as they purpose to intermediate funds between surplus spenders and deficit spenders within East Asia. According to a number of studies conducted in the past, the prosperity of an economy may rise or fall depending on how well the financial markets are doing. The author looked at how the expansion of the East Asian economy is affected by the money markets, corporate and Government Bond markets, and stock markets. In order to estimate the impact that financial market activity, international capital flows, and domestic market capital structure have on East Asian economic development, we include these factors in our model. To get at these findings and suggestions, a content analysis-based systematic literature study on financial markets was conducted. To fully benefit from FDI, governments, particularly in less developed nations, need to strengthen and expand their financial markets. The economy and the global financial system are connected via the financial markets. Direct foreign investment may have a significant impact on host nations' economic growth if their financial systems are well-managed.

Rakib and Hossin (2023) carried out study to examine the impact of Bangladesh's financial market development on the nation's economic growth from 1993 to 2020. The findings were analyzed by means of many different statistical tests, including those for unit roots, cointegration, vector error correction models, and causality. As a consequence, the variables passed the unit root test at first difference. In addition to showing long-term interaction, the vector error correction model confirmed the results of the Johansen cointegration test. The casualty test indicates that there is a one-way causal link between certain variables and another, but not between others. Policymakers in the financial market may use the results of this assessment to inform future efforts by supporting the growth of the financial sector, as suggested by the study's conclusions.

Alakbarov and Murshudova (2020) conducted study to investigate the relationship between financial markets and economic growth in Georgia. Using yearly data from 1995-2017, this research examines the connection between financial development indices, which stand in for financial markets, and GDP, which stands in for economic growth. The Breitung and Candelon

(2006) Frequency Domain Causality Test found that while growth in the economy positively influenced financial market productivity, growth in the financial markets did not cause expansion.

Algaeed (2021) performed study to analyze and test the effects of capital market development on the per-capita GDP growth in Saudi Arabian economy covering the period of 1985-2018. The Johansen, ARDL, and FMOLS tests are all operational. Indicators of the stock market, such as share price index, market capitalization, liquidity, share transactions, and total shares outstanding, are used in conjunction with a log-linear eclectic model tailored to the data at hand. Contrary to the results of a large body of research in economics, negative indicators were seen for capitalization and liquidity. The share price index, volume of trading, and trading volume to volume ratio all showed the predicted positive indicators. The results call into question the effectiveness of the capital market in boosting GDP per capita and the size of the market, as well as the actions and efforts done to develop the capital market. Using the Granger causality test, we find that the stock market's overall index, capitalization, and volume of trading do not granger cause GDP per capita. At the 5 percent level, they are substantial. The CMA should plan how to speed up the process of capital market deepening so that it can better support economic expansion.

3.0 Research Findings and Discussion

The research findings reveal a positive correlation between financial market development and economic growth in Sweden. As the financial market in Sweden has matured and become more sophisticated, it has contributed to the country's sustained economic growth. The well-developed banking system, a highly active stock market, and robust regulatory mechanisms have efficiently channeled capital to various sectors, stimulating investment, productivity, and economic output. Financial market development has significantly impacted entrepreneurship in Sweden. It has provided a platform for startups and innovative companies to raise capital through equity financing. The Stockholm Stock Exchange, with its strong investor base and access to international investors, has been instrumental in supporting entrepreneurship and driving innovation, particularly in the technology sector. Financial market development has been a driver of economic growth, there are concerns related to inclusive growth. There is evidence that the benefits of a well-developed financial sector have not been evenly distributed across all segments of the population. Addressing income inequality and ensuring that the financial market serves the needs of all socioeconomic groups is an ongoing challenge.

The study underscores the importance of Sweden's regulatory framework and investor protection mechanisms in maintaining financial stability. The robust regulatory environment has played a crucial role in preventing systemic risks and ensuring that the expansion of the financial sector does not lead to financial instability. However, it is essential to continuously adapt and strengthen these regulations to mitigate emerging risks. The research highlights sectoral variations in how financial market development impacts different industries. For example, real estate and construction sectors have benefited from lower interest rates due to financial market development, while technology and innovation-driven sectors have seen advantages from access to equity financing. Understanding these sectoral dynamics is essential for tailored policy-making. The findings also emphasize the global interdependence of Sweden's economy. External factors, such as international trade dynamics and global economic conditions, have a significant impact on the relationship between financial market development and domestic economic growth. Researchers and policymakers need to consider these global influences when formulating strategies to maximize the benefits of financial market development.

4.0 Conclusion

As the financial market has matured and diversified, it has contributed significantly to the nation's sustained economic growth. A well-developed banking system, a vibrant stock market, and a regulatory environment that prioritizes investor protection have efficiently allocated capital, encouraged investment, and fostered economic productivity. However, it is essential to recognize that while financial market development has been a driver of growth, there are challenges that should be addressed. Notably, income inequality and the equitable distribution of benefits from the financial sector remain persistent issues. Efforts to ensure that all segments of society can access the opportunities created by financial market development are imperative for a more inclusive growth trajectory.

The study also underscores the significance of a robust regulatory framework in maintaining financial stability. Sweden's regulatory environment has played a vital role in preventing systemic risks and safeguarding against financial crises. As financial markets evolve, policymakers must remain vigilant in adapting and strengthening these regulations to address emerging risks effectively. Sectoral variations in the impact of financial market development have been highlighted. Different industries experience different effects, with real estate and technology sectors serving as prime examples. This underscores the need for tailored policy approaches that account for these sector-specific dynamics. The study emphasizes the global interdependence of Sweden's economy. External factors, such as international trade dynamics and global economic conditions, exert a significant influence on the relationship between financial market development and domestic economic growth. As Sweden navigates a rapidly changing global economic landscape, policymakers and researchers must consider these global factors when crafting strategies to maximize the benefits of financial market development.

5.0 Recommendations

To ensure the sustainability of economic growth in Sweden, it is recommended that policymakers and financial regulators adopt a proactive stance. Continuous monitoring and assessment of the financial sector's expansion are necessary to identify potential risks, including excessive leverage and asset bubbles. Collaborative efforts should be made to strike a balance between promoting financial market development and maintaining financial stability. This might involve implementing countercyclical policies to address economic imbalances and enhancing crisis management tools to mitigate the impact of financial crises. Addressing income inequality and enhancing financial inclusion are critical imperatives. To achieve this, Sweden should promote policies that make financial services more accessible to a broader segment of the population. Encouraging the development of financial technology (FinTech) and mobile banking solutions can provide opportunities for underserved communities to access banking services, savings, and investment options. Financial education programs can empower individuals to make informed financial decisions and participate in the benefits of financial market development.

Recognizing the sectoral variations in how financial market development impacts different industries, Sweden should tailor its policies to address the unique needs of each sector. For instance, supporting SMEs and startups through targeted incentives, including easier access to venture capital and business loans, can foster innovation and entrepreneurship. In parallel, policies to address the challenges associated with real estate, such as housing affordability, should be explored to ensure balanced growth. Given the global interdependence of Sweden's economy, it is essential for the country to remain engaged and adaptable on the international stage. Policymakers should focus on fostering international trade relationships, monitoring global economic conditions, and preparing for potential external shocks. It is advisable to actively participate in global financial governance and regulatory discussions to ensure that Sweden's interests are well-represented.

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