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GRANGER-CAUSALITY BETWEEN MONETARY AGGREGATES
AND SECTORAL PRODUCTION IN MALAYSIA

BY

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ABSTRACT

The main purpose of this study is to empirically assess the distributional impact of financial variables using Malaysian quarterly data. The rationale for pursuing this objective is to identify the possible transmission channels of the financial variables with respect to the sectoral production and its underlying causal. The study employing the methodology of Azali and Habibullah (2000) in using the MWALD test for testing Granger non-causality (Toda Yamamoto, 1995) was constructed using Seemingly Unrelated Regressions (SUR). The Augmented Dickey-Fuller (ADF) and Phillip-Perron (PP) unit root test procedures; Johansen and Juselius (1990) cointegration test and the Toda and Yamamoto (1995) test are conducted to achieve the objectives of the study. This model is use to trace the effects of a monetary shock via the financial variables (i.e. money supply aggregate, commercial loan and stock prices).The results indicate that significant changes in sectoral production differences are found owing to monetary transmissions from financial variables. The empirical results suggest that broad money (M2 and M3) is neutral with respect to the electricity, gas and water (EW) and seemed to have more predicting power in influencing the manufacturing sector. There is neutrality of credit to the production of major services. The findings demonstrate the importance of credit to manufacturing (MF), construction (CS) and government services (GS) in the long run. The results also show that stock market activity has more predictive power in leading agricultural (AG) compared to its impact on the gas and water (EW), wholesale and retail and hotel and restaurants (WR), finance and real estate and business services (FB). In conclusion, the results of this study suggests that money is non-neutral and that it has forecasting power in sectoral production movements in Malaysia.

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