

FINANCIAL DEVELOPMENT AND INCOME INEQUALITY NEXUS IN WEST AFRICAN COUNTRIES: THE MEDIATING ROLE OF TRADE OPENNESS AND INSTITUTIONAL QUALITY

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Abstract

Financial sector development enables more access to financial services and allow a growing number of low-income households and small businesses to participate productively in the formal economy. The study aims to examine the nexus between modern indicators of financial development and income inequality by mediating the role of trade openness and institutional quality in 16 West African countries over the period of 1990 - 2022 using CS-ARDL model. The tests for slope heterogeneity and cross-sectional dependence evidence that the slopes of the regression coefficients are not homogeneous across the cross-sectional units and there is strong cross-sectional dependency among West African countries due to globalization movement, economic cooperation, and labor mobility. The test for panel cointegration evidences the existence of cointegration among the variables, which means there is a stable, long-term relationship among financial development indicators, and income inequality. The result of CS-ARDL reveals that financial access and financial stability significantly improve income distribution while financial efficiency, government expenditure, regulatory quality and corruption control increase income inequality. It also reveals that financial deepening, financial efficiency, and government expenditure increases income inequality. The result also shows that there is bidirectional causality between financial development and inequality. The study concludes that financial access and stability reduce income inequality. It is recommended that there should be increased in access to financial services and products for vulnerable groups of the population, as well as to stabilize the financial institutions and market by reducing high volatility in the price of financial services, product and the stock price index.

Keywords: CS-ARDL Model, Financial Development, Income Inequality, Institutional Quality, Trade Openness, West Africa