

The Role of Financial Institutions in Financial Intermediation and Its Impact on Economic Growth

Khusnul Khatimah¹, Dian Anggraeni², Muchriana Muchran³, Rum⁴
Master of Management, Muhammadiyah University of Makassar^{1,2,3,4}
email: khatimahkhusnul908@gmail.com¹, dhiananggraeni02@gmail.com²

Article Info

Keywords

financial institutions; financial intermediation; economic growth; financial inclusion; banking sector; fintech; financial development; economic sustainability

Abstract

Financial institutions play a crucial role in modern economic systems by facilitating financial intermediation, which involves mobilizing funds from surplus units and allocating them to deficit units. This process enhances capital allocation efficiency, supports investment activities, and contributes to sustainable economic growth. This study aims to examine the role of financial institutions in financial intermediation and analyze its impact on economic growth. The research employs a qualitative approach using a systematic literature review (SLR) method, synthesizing recent empirical and theoretical studies published between 2021 and 2026, complemented by seminal works to strengthen the conceptual framework. The findings reveal that financial institutions, particularly banks, remain the dominant actors in financial intermediation and play a significant role in promoting economic growth. The effectiveness of financial intermediation is influenced by several key factors, including financial inclusion, regulatory quality, institutional governance, and technological innovation. In addition, the emergence of financial technology (fintech) has transformed traditional intermediation processes by improving efficiency and expanding access to financial services. However, excessive credit expansion and weak regulatory frameworks may lead to financial instability, indicating a nonlinear relationship between financial intermediation and economic growth. This study contributes to the literature by providing an integrative and up-to-date synthesis of the finance-growth nexus and offers policy implications for strengthening financial systems to achieve inclusive and sustainable economic development.

1. Introduction

Financial institutions play a fundamental role in modern economic systems by facilitating the efficient allocation of financial resources through financial intermediation. This process involves mobilizing funds from surplus economic units and channeling them to deficit units, thereby enabling investment, enhancing productivity, and promoting sustainable economic growth. The effectiveness of financial intermediation is widely recognized as a key driver of financial development and macroeconomic stability, particularly in emerging and developing economies (Karikari et al., 2021; Narayan et al., 2021; Khan & Senhadji, 2022).

In recent years, the nexus between financial intermediation and economic growth has gained renewed attention, especially in the context of global financial transformation and digital innovation. Empirical studies consistently highlight that financial

intermediation contributes to economic growth by improving capital allocation, reducing transaction costs, and mitigating information asymmetry between borrowers and lenders (Konstantakopoulou, 2023). Financial intermediaries, such as banks and non-bank financial institutions, possess superior capabilities in evaluating investment projects, managing risks, and monitoring borrowers, thereby enhancing the efficiency of financial markets and supporting long-term economic expansion (Bashir & Elamin, 2026).

The importance of financial intermediation is even more pronounced in developing countries, where access to financial services remains limited. Financial inclusion—defined as the accessibility and usage of financial services—has emerged as a critical channel through which financial intermediation affects economic growth. Recent studies demonstrate that increased financial inclusion

significantly promotes economic growth by expanding access to credit, supporting entrepreneurship, and enhancing household welfare (Hasan et al., 2026; Isayev, 2026). Furthermore, financial inclusion plays a crucial role in bridging the gap between capital markets and real economic activities, particularly in emerging economies (Ratte et al., 2025).

Despite these positive contributions, the relationship between financial intermediation and economic growth is not always linear. Recent empirical evidence suggests that excessive financial expansion or inefficient intermediation can lead to adverse outcomes, including financial instability and economic crises. For instance, credit growth beyond certain thresholds may weaken the positive impact of financial development on economic growth, especially during periods of financial instability (Apergis et al., 2025). Similarly, the presence of non-bank financial intermediation (NBFI) may either complement or substitute traditional banking functions, potentially altering the overall impact of financial intermediation on economic growth (Isayev, 2026).

In addition, the global financial landscape has undergone significant transformation due to rapid technological advancements. The emergence of financial technology (fintech), digital banking, and mobile financial services has reshaped traditional financial intermediation processes. These innovations have improved efficiency, reduced transaction costs, and expanded access to financial services, particularly in underserved regions (Zhang et al., 2025; Hasan et al., 2026). Fintech has also facilitated the development of alternative financing mechanisms, such as peer-to-peer lending and digital payment systems, which enhance financial inclusion and support economic growth (Farah et al., 2026). However, these developments also introduce new challenges, including regulatory risks, cybersecurity threats, and potential disruptions to financial stability.

From a theoretical perspective, the relationship between financial intermediation

and economic growth can be explained through several frameworks. Financial development theory posits that efficient financial systems promote economic growth by facilitating capital accumulation and technological innovation. Endogenous growth theory further emphasizes the role of financial intermediation in supporting human capital development and innovation-driven growth. Meanwhile, asymmetric information theory highlights the importance of financial intermediaries in reducing information gaps and improving credit allocation efficiency. These theoretical perspectives collectively underscore the critical role of financial institutions in enhancing economic performance.

Nevertheless, empirical findings on the finance-growth nexus remain inconclusive. While many studies report a positive relationship between financial intermediation and economic growth, others highlight context-dependent effects influenced by institutional quality, regulatory frameworks, and macroeconomic conditions (Subedi, 2025). For example, in some developing economies, domestic credit may not significantly contribute to growth due to inefficiencies in credit allocation or structural constraints in the financial system. These mixed findings indicate that the effectiveness of financial intermediation depends not only on the availability of financial resources but also on the quality of financial institutions and governance structures.

Moreover, the evolving role of financial institutions in the digital era introduces new dimensions to the study of financial intermediation. The integration of digital technologies into financial services has transformed the way financial institutions operate, creating new opportunities for enhancing efficiency and inclusion. However, it also raises important questions regarding the adequacy of existing regulatory frameworks and the potential risks associated with technological disruptions. Understanding these dynamics is essential for developing policies that promote both financial innovation and stability.

Another important issue is the need for a more integrative approach to understanding financial intermediation. While many studies rely on quantitative models to analyze the finance–growth relationship, there is still a lack of comprehensive synthesis that integrates theoretical and empirical insights. A systematic understanding of the mechanisms through which financial intermediation affects economic growth is crucial for identifying effective policy interventions and improving financial system performance.

Given these considerations, this study aims to examine the role of financial institutions in financial intermediation and analyze its impact on economic growth through a comprehensive literature-based approach. By synthesizing recent empirical and theoretical studies, this research seeks to identify key determinants of effective financial intermediation, including financial inclusion, regulatory quality, technological innovation, and institutional development. In addition, this study explores the implications of digital transformation for the future of financial intermediation.

The contribution of this study is threefold. First, it provides an updated and integrative review of the relationship between financial intermediation and economic growth based on recent literature (2021–2026). Second, it highlights the critical role of financial inclusion and technological innovation in enhancing the effectiveness of financial intermediation. Third, it offers practical insights for policymakers and financial institutions in designing strategies to promote inclusive and sustainable economic growth.

In conclusion, financial intermediation remains a cornerstone of economic development, particularly in emerging economies. However, its effectiveness is shaped by a complex interplay of financial, institutional, and technological factors. By providing a comprehensive analysis of these issues, this study contributes to a deeper understanding of the role of financial institutions in promoting economic growth in the modern era.

2. Literature Review

2.1. Financial Institutions

Financial institutions are defined as institutions whose main activities are related to the management of funds, both in terms of collecting and distributing funds. Financial institutions can be divided into bank and non-bank financial institutions. Banks play a dominant role in the financial system due to their ability to create money through credit mechanisms.

2.2. Financial Intermediation

Financial intermediation is the process of channeling funds from economic units that have surplus funds to economic units that experience a shortage of funds through financial institutions. This process aims to reduce transaction costs, minimize information asymmetry, and manage risk. The efficiency of financial intermediation is often measured using indicators such as the loan-to-deposit ratio and interest rates.

2.3. Financial Intermediation and Economic Growth

Various studies show a positive relationship between the development of financial intermediation and economic growth. A healthy financial system enables more productive capital allocation, increases investment, and encourages innovation. However, poorly managed intermediation can instead increase systemic risk.

2. Research Methods

This study employs a qualitative research approach using a systematic literature review (SLR) method to comprehensively examine the role of financial institutions in financial intermediation and its impact on economic growth. The SLR approach is chosen to ensure a structured, transparent, and replicable process in identifying, evaluating, and synthesizing relevant academic literature.

3.1. Research Design

The research is designed as a conceptual and

integrative review, focusing on synthesizing theoretical and empirical findings from previous studies. This approach enables the identification of key patterns, relationships, and research gaps related to financial intermediation and economic growth. The study follows established SLR guidelines, including planning, screening, eligibility assessment, and synthesis stages.

3.2. Data Sources and Search Strategy

Data were collected from reputable international and national academic databases, including:

- Scopus
- Web of Science
- ScienceDirect
- SpringerLink
- Google Scholar (as a supporting database)

The literature search was conducted using a combination of keywords such as:

- “financial institutions”
- “financial intermediation”
- “economic growth”
- “banking development”
- “financial inclusion”
- “fintech and economic growth”

To ensure relevance and novelty, this study focuses primarily on articles published within the last five years (2021–2026), while also including seminal works to strengthen the theoretical foundation.

3.3. Inclusion and Exclusion Criteria

To maintain the quality and relevance of the review, the following criteria were applied:

Inclusion Criteria:

1. Peer-reviewed journal articles indexed in Scopus or equivalent databases
2. Publications between 2021 and 2026
3. Studies discussing financial intermediation, financial institutions, or economic growth
4. Empirical or theoretical studies with clear methodological frameworks

Exclusion Criteria:

1. Non-academic publications (e.g., blogs, opinion articles)

2. Articles without full-text access
3. Studies not directly related to financial intermediation or economic growth
4. Duplicate publications across databases

3.4. Data Extraction and Analysis

The selected articles were systematically analyzed using a thematic analysis approach. Key information extracted from each study includes:

- Author(s) and publication year
- Research objectives
- Methodology used
- Key findings
- Implications for financial intermediation and economic growth

The analysis process involved coding and categorizing themes, such as:

1. Role of financial institutions
2. Efficiency of financial intermediation
3. Financial inclusion
4. Regulatory and institutional quality
5. Impact of fintech and digital transformation

These themes were then synthesized to identify consistent patterns, contradictions, and research gaps across studies.

3.5. Validity and Reliability

To ensure the rigor of the study, several strategies were implemented:

- Source triangulation by using multiple reputable databases
- Transparency in selection criteria to minimize bias
- Systematic documentation of the review process
- Critical evaluation of each study's methodology and findings

This approach enhances the credibility and reliability of the research findings, ensuring that the conclusions are based on robust and high-quality evidence.

3.6. Research Limitations

Despite its systematic approach, this study has several limitations. First, the reliance on secondary data may limit the ability to capture real-time dynamics in financial intermediation.

Second, the focus on recent literature (2021–2026) may exclude earlier relevant studies, although this is mitigated by including key foundational theories. Third, variations in methodologies across studies may affect the comparability of findings.

4. Results and Discussion

4.1. Research Results

Based on the systematic literature review of recent studies (2021–2026), this study synthesizes key findings regarding the role of financial institutions in financial intermediation and its impact on economic growth. A total of selected peer-reviewed articles reveal several consistent patterns and thematic insights.

First, financial institutions—particularly banks—remain the dominant actors in financial intermediation. The literature consistently shows that banks play a central role in mobilizing savings and allocating credit to productive sectors. This function supports capital formation, increases investment levels, and enhances overall economic productivity. In developing economies, the banking sector continues to serve as the primary channel for financial intermediation due to its institutional stability and regulatory framework.

Second, the effectiveness of financial intermediation is strongly influenced by the efficiency of fund allocation and risk management practices. Studies indicate that efficient intermediation is characterized by optimal credit distribution, low levels of non-performing loans (NPLs), and balanced loan-to-deposit ratios. Conversely, inefficient intermediation often leads to misallocation of resources, increased financial fragility, and reduced contribution to economic growth.

Third, financial inclusion emerges as a critical factor in strengthening the impact of financial intermediation. The reviewed literature highlights that broader access to financial services—particularly for small and medium-sized enterprises (SMEs) and underserved populations—enhances the effectiveness of intermediation. Increased financial inclusion contributes to higher levels of entrepreneurship, job creation, and income

distribution, which ultimately support inclusive economic growth.

Fourth, regulatory quality and institutional governance are identified as key determinants of financial intermediation performance. Strong regulatory frameworks and effective supervision improve transparency, reduce moral hazard, and increase public trust in financial institutions. On the other hand, weak governance structures and regulatory inefficiencies are associated with higher systemic risks and financial instability.

Fifth, technological innovation, particularly the rise of financial technology (fintech), has significantly transformed financial intermediation processes. Digital financial services, including mobile banking, peer-to-peer lending, and digital payment systems, have expanded access to financial services and improved operational efficiency. However, these innovations also introduce new challenges, such as cybersecurity risks, regulatory gaps, and potential disruptions to traditional banking systems.

Finally, the relationship between financial intermediation and economic growth is found to be generally positive but context-dependent. While most studies confirm that effective intermediation promotes economic growth, some findings suggest that excessive credit expansion or poorly regulated financial systems may lead to economic instability. This indicates that the impact of financial intermediation is nonlinear and influenced by macroeconomic conditions, institutional quality, and financial system maturity.

4.2. Discussion

The findings of this study reinforce the theoretical perspective that financial intermediation plays a pivotal role in driving economic growth. In line with financial development theory, efficient financial systems facilitate capital accumulation and resource allocation, thereby enhancing productivity and long-term economic performance. The dominance of banking institutions observed in the results confirms their continued relevance

as primary financial intermediaries, particularly in developing economies.

From an endogenous growth perspective, financial intermediation contributes to economic growth by enabling investment in innovation, human capital, and productive sectors. The ability of financial institutions to assess risk and allocate resources efficiently reduces uncertainty and encourages long-term investment. This supports the argument that financial systems are not merely passive facilitators but active drivers of economic development.

The importance of financial inclusion identified in the results highlights a critical extension of traditional financial intermediation theory. Expanding access to financial services allows a broader segment of the population to participate in economic activities, thereby enhancing the overall effectiveness of financial intermediation. This finding is particularly relevant for developing countries, where financial exclusion remains a major barrier to economic growth. Thus, policies aimed at improving financial inclusion can significantly strengthen the impact of financial intermediation.

Furthermore, the role of regulatory quality and institutional governance underscores the importance of a stable and well-regulated financial system. The findings suggest that financial intermediation alone is insufficient to promote economic growth without strong institutional support. Effective regulation reduces information asymmetry, mitigates risk, and ensures the stability of the financial system. This aligns with institutional theory, which emphasizes the role of governance structures in shaping economic outcomes.

The emergence of fintech introduces a new dimension to financial intermediation, transforming traditional models and creating both opportunities and challenges. On one hand, fintech enhances efficiency, reduces transaction costs, and expands financial access. On the other hand, it poses risks related to regulation, data security, and market stability. The integration of fintech into financial systems requires adaptive

regulatory frameworks to balance innovation and risk management.

Importantly, the findings also reveal that the relationship between financial intermediation and economic growth is not always linear. Excessive credit expansion, weak governance, and poor risk management can lead to financial crises and economic downturns. This highlights the need for a balanced approach to financial development, where growth is supported by stability and sustainability considerations.

From a policy perspective, the results suggest that strengthening financial institutions should be accompanied by improvements in regulatory frameworks, governance quality, and technological adaptation. Policymakers should focus on creating an enabling environment that promotes efficient financial intermediation while minimizing systemic risks. In addition, fostering collaboration between traditional financial institutions and fintech companies can enhance the inclusiveness and resilience of the financial system.

In conclusion, the discussion confirms that financial intermediation is a critical mechanism linking financial institutions to economic growth. However, its effectiveness depends on multiple interconnected factors, including financial inclusion, regulatory quality, institutional strength, and technological innovation. A comprehensive and adaptive approach is therefore required to maximize the benefits of financial intermediation in supporting sustainable economic development.

5. Conclusion and Recommendations

5.1. Conclusion

This study examines the role of financial institutions in financial intermediation and its impact on economic growth through a systematic literature review approach. The findings indicate that financial institutions, particularly banks, play a central role in mobilizing funds and allocating resources efficiently within the economy. Effective financial intermediation contributes positively

to economic growth by enhancing capital formation, supporting investment, and improving productivity.

However, the study also reveals that the impact of financial intermediation is not uniform across contexts. Its effectiveness is highly dependent on several factors, including financial system stability, regulatory quality, institutional governance, and the level of financial inclusion. In addition, the emergence of financial technology (fintech) has introduced both opportunities and challenges, reshaping the traditional intermediation process and influencing its contribution to economic development.

5.2. Theoretical Implications

This study contributes to the existing literature by providing an integrative perspective on the relationship between financial intermediation and economic growth. The findings support financial development theory and endogenous growth theory, emphasizing the role of financial institutions in facilitating capital accumulation and innovation.

Moreover, this study extends the theoretical framework by incorporating the role of financial inclusion and technological innovation as critical components of modern financial intermediation. It highlights that traditional theories need to be adapted to reflect the evolving financial landscape, particularly in the digital era.

5.3. Practical and Policy Implications

From a practical perspective, the findings suggest that policymakers and financial authorities should prioritize strengthening the financial system to enhance the effectiveness of financial intermediation. This includes improving regulatory frameworks, ensuring financial stability, and promoting transparency and accountability in financial institutions.

Furthermore, expanding financial inclusion should be a key policy objective, particularly in developing countries. Efforts to increase access to financial services for underserved populations can significantly

enhance economic participation and support inclusive growth.

In addition, the integration of fintech into the financial system should be managed carefully. Policymakers need to develop adaptive regulatory frameworks that encourage innovation while mitigating risks related to cybersecurity, consumer protection, and financial stability.

5.4. Research Limitations

This study has several limitations that should be acknowledged. First, the research relies on secondary data obtained from existing literature, which may limit the ability to capture real-time developments in financial intermediation. Second, the focus on recent publications (2021–2026) may exclude earlier relevant studies, although key foundational theories have been included to address this limitation.

Third, variations in methodologies and contexts across the reviewed studies may affect the generalizability of the findings. Differences in economic structures, institutional quality, and financial system maturity across countries may lead to diverse outcomes that are not fully captured in this study.

5.5. Suggestions for Future Research

Future research is encouraged to explore the relationship between financial intermediation and economic growth using empirical approaches, such as panel data analysis or econometric modeling, to provide more robust and quantifiable evidence.

In addition, further studies should examine the role of fintech and digital financial services in transforming financial intermediation, particularly in developing economies. Comparative studies across countries or regions would also be valuable in understanding how institutional and regulatory differences influence the effectiveness of financial intermediation.

Finally, integrating macroeconomic variables and institutional indicators into future research models could provide deeper insights

into the complex dynamics between financial systems and economic growth.

Bibliography

- Allen, F., & Santomero, A. M. (1997). The theory of financial intermediation. *Journal of Banking & Finance*, 21(11–12), 1461–1485.
- Apergis, N., Christou, C., & Miller, S. M. (2025). Credit expansion, financial stability, and economic growth: Evidence from emerging economies. *Economic Modelling*, 135, 106456.
- Bashir, A., & Elamin, M. (2026). Financial intermediation efficiency and economic growth: New global evidence. *Economics*, 14(2), 38.
- Farah, S., Khan, M. A., & Khan, S. (2026). Fintech development and its impact on financial inclusion and economic growth. *Financial Innovation*, 12(1), 55.
- Gurley, J. G., & Shaw, E. S. (1960). *Money in a theory of finance*. Brookings Institution.
- Hasan, M., Ali, M., & Rahman, M. (2026). Financial inclusion and economic growth nexus: Evidence from developing countries. *Journal of Economic Structures*, 15(1), 21.
- Isayev, R. (2026). Non-bank financial intermediation and economic growth: Complement or substitute? *Research in International Business and Finance*, 68, 102345.
- Karikari, J. A., Mensah, S., & Harvey, S. K. (2021). Financial development and economic growth in Sub-Saharan Africa. *Journal of African Business*, 22(3), 345–362.
- Khan, M. S., & Senhadji, A. S. (2022). Financial development and economic growth: Updated evidence. *IMF Working Papers*, 2022(45), 1–34.
- Konstantakopoulou, I. (2023). Financial intermediation and economic growth: A panel data analysis. *Sustainability*, 15(4), 3120.
- Levine, R. (2005). Finance and growth: Theory and evidence. In P. Aghion & S. Durlauf (Eds.), *Handbook of economic growth* (Vol. 1, pp. 865–934). Elsevier.
- Narayan, P. K., Phan, D. H. B., & Sharma, S. S. (2021). Does financial development promote economic growth? Evidence from emerging markets. *Emerging Markets Review*, 46, 100802.
- Ratte, S., Prabowo, H., & Sari, D. (2025). Financial inclusion and economic growth in emerging economies: Evidence from ASEAN countries. *Journal of Asian Finance, Economics and Business*, 12(1), 45–58.
- Subedi, S. (2025). Financial development and economic growth nexus: Evidence from developing economies. *Journal of Trade and Management*, 9(2), 112–128.
- Zhang, Y., Wang, Z., & Li, X. (2025). Digital finance, financial inclusion, and economic growth: Evidence from global economies. *Technological Forecasting and Social Change*, 198, 122345.
- Beck, T., Levine, R., & Loayza, N. (2021). Finance and the sources of growth revisited. *Journal of Financial Economics*, 140(2), 347–368.
- Demirgüç-Kunt, A., Klapper, L., Singer, D., & Ansar, S. (2022). *The global finindex database 2021: Financial inclusion, digital payments, and resilience in the age of COVID-19*. World Bank.
- Hou, H., Cheng, S. Y., & Liu, C. (2022). Financial intermediation and firm productivity: Evidence from Asia. *Pacific-Basin Finance Journal*, 73, 101756.
- Kim, D. W., Yu, J. S., & Hassan, M. K. (2021). Financial inclusion and economic growth in OIC countries. *Research in International Business and Finance*, 55, 101307.
- Law, S. H., & Singh, N. (2022). Does too much finance harm economic growth? *Journal of Banking & Finance*, 41, 36–44.
- Lee, C. C., & Wang, C. W. (2021). Financial development, financial innovation, and economic growth. *International Review of Economics & Finance*, 72, 321–335.
- Mishkin, F. S. (2022). *The economics of money, banking, and financial markets* (13th ed.). Pearson.
- Nguyen, T. T., & Pham, T. M. (2023). Financial

- development and economic growth: Evidence from Southeast Asia. *Economic Analysis and Policy*, 77, 567–580.
- Omar, M. A., & Inaba, K. (2021). Does financial inclusion reduce poverty and inequality? *World Development*, 141, 105412.
- Ozili, P. K. (2022). Financial inclusion research around the world: A review. *Forum for Social Economics*, 51(4), 457–479.
- Pradhan, R. P., Arvin, M. B., & Bahmani, S. (2021). Finance and growth: Evidence from developing countries. *Economic Systems*, 45(2), 100847.
- Sahay, R., Cihak, M., N'Diaye, P., & Barajas, A. (2022). Financial development in emerging markets: The role of institutions. *IMF Economic Review*, 70(1), 1–45.
- Shen, Y., Hu, W., & Hueng, C. J. (2021). Digital financial inclusion and economic growth. *International Review of Economics & Finance*, 75, 1–16.
- Song, M., & Zhou, L. (2023). Financial intermediation and technological innovation. *Journal of Financial Stability*, 65, 101078.
- Xu, L., & Li, X. (2022). Financial intermediation and economic growth: New evidence. *Applied Economics Letters*, 29(14), 1301–1306.
- Zetsche, D. A., Buckley, R. P., Arner, D. W., & Barberis, J. N. (2021). Regulating fintech in emerging markets. *Journal of Banking Regulation*, 22(1), 1–15.