

Effects of public debt on economic growth of East African countries

Victor Muoki
KCA University
Nairobi
victormuoki@yahoo.com

Olanrewaju Isola Fatoki
KCA University
Nairobi
lanrefatoki@kca.ac.ke

Abstract

The purpose of this study was to determine the influence of public debt on economic growth of three east African countries (Kenya, Uganda and Tanzania). Specifically, the study aimed to establish the influence of external concessional public debt, external commercial public debt and domestic public debt on economic growth of the three east African countries. This study applied a causal research design as it sought to assess effect of public debt on economic growth and collect secondary time series data for 57 years (1963 – 2019). Macro panel regression was used to analyze the collected data using the fixed effects model. The study findings established that concessional debt and external commercial debt had a significant positive effect on economic growth, while domestic debt had a significant negative effect on economic growth. Based on this study findings, the study makes the following recommendations. First, the three East African countries should source for more external concessional debt through bilateral or multilateral arrangements to plug into their budget deficits. The study also recommends that the level of domestic borrowing in the three East African countries should be reduced. This is because domestic borrowing is harmful to economic growth of the three countries.

Key words: *Public debt, External debt, Domestic debt, Concessional, Commercial, Economic growth.*

1.Introduction

Practically all governments globally have expenditures that surpass their revenues and hence experiencing budget deficits. These jurisdictions could improve their revenues by printing money, increasing tax revenues, engaging in external or domestic borrowing, or using prior period's budget surpluses if available(Onafowora & Owoye, 2019). Due to the inappropriateness of the other measures of addressing budgets deficits due to their negative outcomes, governments mostly resort to borrowing which creates financial obligations referred to as public debt(Arčabić et al., 2018).There are various options available to a government when it comes to borrowing to finance budget deficits. These include borrowing from external sources, borrowing domestically from commercial banks, borrowing from its central or federal bank (comparable to money printing) or borrowing from domestic financial entities (Gmez-Puig & Sosvilla, 2017). Each of the available alternatives have differing effects on the economy and present various short-term or long-term implications.

Rather than borrowing from a single source, governments usually combine debt from different sources in a mixeddebt strategy. This is done to maximize the benefits while reducing risks appertaining to the different debt sources. Various governments globally have resulted to financing their fiscal deficits by issuing bonds and bills, externally and domestically since expanding tax bases or growing money supply are limited by statutory provisions(Amann & Middleditch, 2017).Foreign and domestic debt are largely applied in developing countries that have key deficiencies in capital formation in their private sectors(Mhlaba & Phiri, 2019). There are various economic and political studies over the years that have hotly debated the influence of public debt on economic growth of developed and developing countries.

Economic growth is the ability of an economy to produce services and goods in a given year compared to the preceding year. This is mostly measured in terms of gross domestic product or gross national product(Chudik et al., 2018).According to Maisonnave, Chitiga, Mabugu and Decaluwé (2015), public debt can improve the national productivity and employment opportunities in the economy if it is applied to be factors of production such as machinery, technology and knowhow. This concept is supported by the works of early scholars as indicated byPegkas (2018), who provided the groundwork for the advancement of an all-inclusive theory of development, economic growth and debt.These scholars had a common perspective that transfer of resources from foreign sources (through grants, aid or loans) to developing and less developed nations could lead to economic transformation in the recipient countries through enhancing their growth rates from negative and low levels to sustainably high growth levels (Chiu & Lee, 2017). Thecontributions of these scholars and other proponents with similar perspectives indicate that public debt to developing countries is critical as its purpose is to supplement the limited domestic resources with positive influences on the economy.

The significance of the early proponents of the positive influence of public debt on economic growth is that public debt at reasonable levels can enhance economic growth (Mousa & Shawareh, 2017). Moreover, since least developed countries are in the early stages of development, they lack sufficient capital to invest in the numerous opportunities which exist. This is unlike the case in developed countries where the expected rate of return is lower than in the developing or emerging economies (Guei, 2019). Therefore, as long as these emerging and developing economies use the borrowed funds effectively in productive sectors, they will reap greater returns than the cost of the funds, which will enhance economic growth (Pegkas, 2019). This concept explains why economic growth and public debt have a short-term positive relationship for the countries with reasonable debt levels.

The shortcomings of the early contributions regarding public debt and economic growth is that, the concepts of crowding out or debt overhang are not explained (Liu & Lee, 2018). Based on these limitations of the early contributions, contemporary theories of public debt and economic growth have been formulated. Krugman (1988) is one of the key contributors explaining the long-term effect of public debt on economic growth through the overhang hypothesis. This has informed several theoretical perspectives on the negative effects of public debt on economic growth (Reinhart, Reinhart, & Rogoff, 2015; Chiu & Lee, 2017; Saungweme & Odhiambo, 2018).

Informing this perspective is Krugman (1988) who developed the concept of “debt overhang” as a state where a country’s capacity to repay debt and the positive effect of the debt on the economy is lower than the contractual value of the debt. Moreover, there are situations where public debt can have adverse effects on the economy depending on where the debt has been invested and due to crowding out. This is when too much government involvement in the capital and financial markets reduces the funds available for the private sector and hence reducing investments (Akram, 2011). Besides, Cohen’s (1993) theoretical model implies a non-linear effect of foreign borrowing on economic growth. Thus, up to a certain level, accumulation of foreign debt is expected to promote economic growth. However, beyond this level, debt overhang applies and the debt exerts negative pressure on the willingness of investors to provide more capital and hence negatively impacting economic growth.

Borrowed funds if properly used can significantly assist a country and contribute to its economic growth. Nevertheless, the influence of public debt on economic growth of various countries have provided diverse and contradicting findings. For instance, a study by Chiu and Lee (2017) on 61 countries around the globe established that public debt has varying influences on economic growth depending on the risk environment of the country. In countries with high financial, economic and political risk, public debt has been reported to negatively influence economic growth while the opposite is true in countries with low risks. These findings contradicted previous findings by Checherita-Westphal and Rother (2011) in a study on 12 European Union (EU) countries which established that public debt has an inverted U-

shape relationship with economic growth. Further, the study determined that the turning point of public debt to GDP ratio was between 90 and 100%.

East Africa countries (Kenya Uganda and Tanzania) have been relying on public debt to bridge budget deficits. They have been combining various components of public debt (concessional, commercial and domestic). In Kenya, public debt as a ratio of GDP reached its highest level in 2000 when it was 78% of GDP. However, efforts were made and it was gradually reduced to its lowest point in 2012 of 39%. However, from 2012, Kenya's public debt has increased steadily to a ratio of 62.1% recorded in 2019. In Uganda there has been notable changes in the debt to GDP ratio over the years. The ratio reached its highest level in 2003 at 72%. However, measures were taken to reduce the ratio to its lowest level at in 2009 at 20%. From 2009 to 2018, the level has increased steadily to 40%. Tanzania's debt to GDP levels have also experienced major disruptions over the years. The highest recorded level was in 2000 when the public debt to GDP levels were 50%. This was reduced steadily to its lowest levels in 2008 (22%). However, from 2008, the levels of debt to GDP have risen steadily to its 2018 level of 37.5%. Among the east African countries, Tanzania has the lowest current level of debt to GDP ratio.

1.1 Statement of the Problem

The global financial crisis was followed by an immense surge in public sector borrowing. Globally, total outstanding public debt increased to \$70 trillion at the end of 2018 from \$35 trillion recorded in 2007. Over similar period, public debt increased to 102% of gross domestic debt (GDP) from 70% in developed countries and to 50% of GDP from 35% in developing and emerging economies (Whajah et al., 2019). In Kenya, public debt as a percentage of GDP increased to 62% at the end of 2019 from 31% in 2010 (CBK, 2020). In Uganda, public debt as a ratio to GDP is at 40% with Tanzania experiencing a debt to GDP ratio of 38%. Though debt to GDP ratios have been increasing, GDP growth has mostly stagnated in the three countries. This fast surge in public debt has stimulated much debate regarding the effects of public debt on the different economies globally (Liu & Lee 2018; Butkus & Seputiene, 2018; Djiogap, 2017).

Though public debt is critical in bridging budget deficits, sustained high debt to GDP ratio can have negative effects on the economy in the long term (Saungweme & Odhiambo, 2018). Large sustained budget deficits could crowd out private investment and lead to fiscal imbalances and thus negatively affecting economic growth. Chudik, Mohaddes, Pesaran and Raissi (2018) observed that the relationship between economic growth and public debt is complex as it varies across countries and influenced by global factors. Various scholars have attempted to determine the effect of public debt on economic growth of different countries globally. Mhlaba and Phiri (2019) established that public debt has a long-term negative association with South Africa's economic growth. Another study by Chiu and Lee (2017) established that the effect of public debt is influenced by the risk environment of the country. In Jordan,

Mousa and Shawareh (2017) established that public debt has a negative relationship with economic growth. In Kenya, Musyoka (2017) determined that public debt has an adverse influence on economic growth in Kenya while Achwoga (2016) established that economic growth is negatively and significantly associated with both domestic and external debt. Another study by Kobey (2016) established that public debt had a negative relationship with economic growth, but had no significant effect on economic growth. These studies used time series regression to assess the influence of public debt on economic growth while the current study applied macro panel data and performed dynamic panel data analysis to assess how public debt of three east African countries influence economic growth.

1.2 Research Hypotheses

The study tested the following hypotheses;

- H₀₁: External concessional public debt has no significant effect on economic growth of three east Africa countries
- H₀₂: External commercial public debt has no significant effect on economic growth of three east Africa countries
- H₀₃: Domestic debt has no significant effect on economic growth of three east Africa countries

2. Literature Review

2.1 Theoretical Review

The study was based on three theories. These are the Keynesian theory, debt overhang hypothesis and crowding out theory. The proponents of these theories, the years these theories were developed and the application of the theories in the study are provided in the following sections. The Keynesian theory was developed by Keynes (1936) and its key proposition is that there is no real burden associated with public debt and government involvement in economic activities. The theory proposes that public borrowing is not damaging to the economy as indicated by classical economists but it contributes to the smooth functioning of the economy by reducing imbalances (Yolcu, 2018). It is therefore expected that if well managed, public debt will spur economic growth (Shahor, 2018). This is because public debt is expected to involve the government in value adding activities and thus adding to national wealth and the growth of the country as a whole.

Krugman (1988) created the “debt overhang” concept as a state in which the external debt repayment ability of the country falls below the contractual value of public debt. This theory posits that public debt burdens the country as many countries invest the funds in investments with lower returns than the interest on those debts. This makes the debt to have adverse effects on the economy. Cohen’s (1993)

theoretical model supported this by indicating a non-linear effect of public borrowing on economic growth and investment. Therefore, up to a certain level, accumulation of public debt could promote investment and economic growth. However, beyond that level, accumulation of more debt will have negative effects on investments and economic growth due to debt overhang.

The crowding out theory dates back to the 1970s after the seminal works of Bacon and Eltis (1976). The authors argued that increased government involvement in the financial and market economy adversely affects the remainder of the market. The theory when applied to domestic borrowing hypothesizes that increased government domestic debt leads to a shortage of funds for the private sector leading to rise of interest rates and thus negatively affecting private investments. The economic situation in the country influences the extent of government's domestic debt crowding out private investments. For instance, Spilioti and Vamvoukas (2015) note that when the economy is at full employment or capacity, increase in government borrowing creates competition for scarce funds between private sector and the public sector. This in turn leads to a rise in interest rates, reduced access of funds by the private sector and hence reduced private consumption and investment. This results to a decrease in economic growth (Mhlaba & Phiri, 2019).

2.2 Empirical Review

A study by Casares (2015) assessed the influence of public debt on economic growth. The research presents an endogenous growth model which incorporates non-tradable and tradable goods. According to the author, external debt can have a non-linear impact on a county's economic growth. When the indebtedness is high, an increase in the proportion of external debt to GDP hurts the economy while when the indebtedness is low, the increase in proportion promotes economic growth (Casares, 2015). The findings are supported by Kobey's (2016) study that proportion external debt and debt servicing have a significant influence on the economic growth within the country.

Ngugi's (2016) research sought to investigate the impact of public debt on the Kenyan economic growth pattern. The study included data collected between 1983 and 2013 which was analysed through the causal research design to derive the findings. From the study results, external debts, lagged GDP, private investment, and real exchange rates had a positive impact on the economic growth. A similar study by Saungweme and Odhiambo (2018) posit that there is inconsistent evidence on the effect of external public debt on the economic growth. The systematic review concludes that foreign debts can have varying impact on GDP growth depending with the level of indebtedness.

A study by Ejigayehu and Persson (2013) examined whether external debts influences economic growth of heavily indebted poor African states through debt crowding out and overhang effect. The findings of the study show that external debts influence the economic growth through debt crowding

which relates to debt servicing. A corresponding research by Atique and Malik (2012) investigated the influence of domestic and external debts on Pakistan's GDP growth. The findings of the study show that the relationship between external debt and economic growth is inverse. The level of external debts slows down the growth as compared to domestic debts and its impact is stronger.

Kamundia (2016) affirms that commercial external debt has higher interest rates which increase the level of indebtedness for emerging economies. According to the author, the primary debt burden for developing and under-developed states lies on commercial debts that are incurred at high annual interest charges. The high demands of commercial external borrowing increase the interest rates thus negatively affecting economic growth. Matiti (2013) supports this argument that shallow economies result to increased commercial borrowing after they exhaust concessional finance.

Ncanywa and Masoga (2018) investigated the role of public debt in stimulating public investment and economic development in South Africa. According to the researchers, high-interest rates have an adverse effect on GDP growth. Ncanywa and Masoga (2018) findings reveal that high interests on commercial external debt result in high debt costs which force the government to impose more taxations. The outcome of this is reduced finances for investment and sluggish economic growth. Casares (2015) supports Ncanywa and Masoga's (2018) argument that high-interest rates on commercial external debt induce deficits on current account and forces states to borrow more.

Njoroge's (2015) research investigated the relationship between government domestic borrowing and economic growth in Kenya. The research used quarterly data from 2003 to 2013. From the findings, the total domestic debt was \$53.4 billion out of a total of 61 billion dollars. Njoroge (2015) established that there is no causal effect on the economic growth resulting from domestic borrowing. Another study by Ebi, Abu, and Clement (2013) examined the potency of domestic and foreign debts on the performance of the Nigerian economy. Time series data between 1970 and 2011 was derived from secondary sources. From the study results, domestic debts have an adverse effect on the country's ability to grow economically.

2.3 Conceptual Framework

The study was based on the conceptual framework presented in Figure 1. The independent variables in the study are public debt components (external concessional debt, external commercial debt and domestic debt). The dependent variable is economic growth measured using real GDP growth rate.

Independent variables

Dependent variable

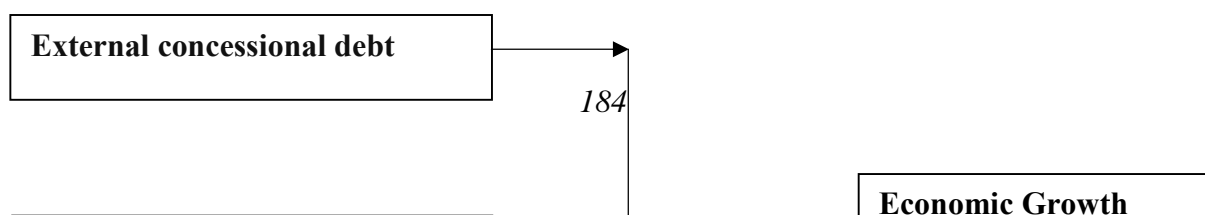


Figure1: Conceptual Framework

3. Methodology

This study applied a causal research design as it sought to collect secondary dynamic panel data to establish the relationship between public debt and economic growth. According to Pischke and Angrist (2014), a causal research design is appropriate when one seeks to assess the relationship that exists between variables observed overtime or the cause and effect relationship amongst the study variables. The study focussed on Kenya, Uganda and Tanzania. These were selected as they are the leading economies in East Africa and at the same time, they have recorded high and growing debt to GDP ratios. The study focussed on available data for the countries for 57 years (1963 – 2019). The secondary data that was used in this study was collected from the World Bank, Kenya National Bureau of Statistics (KNBS), Central Bank of Kenya (CBK), National Bureau of Statistics, Bank of Tanzania, Uganda Bureau of Statistics and Bank of Uganda.

Macro panel data regression model was used in the analysis of the data as the time dimension was greater than the number of entities. Before analyzing the data through the model, the data were explored using descriptive statistics (mean and standard deviations) and trend analysis. This was through the aid of Stata statistical software version 15. The macro panel data regression model (fixed effects) was applied. This enabled the testing of the role of the independent variables (external concessional debt, external commercial debt and domestic public debt) on economic growth. A Hausmann test was conducted which established that the fixed-effects model was appropriate for the data.

The empirical model was of the form;

$$Y_{it} = \beta_1 X_{1it} + \beta_2 X_{2it} + \beta_3 X_{3it} + \varepsilon_{it} \dots\dots\dots (i)$$

Where,

Y = Economic growth

X_1 = External concessional debt

X_2 = External commercial debt

X_3 = Domestic public debt

t = time period (1963 - 2019)

i = Country (Kenya Uganda and Tanzania)

ε_t = error term

Panel data diagnostics (test for multicollinearity, heteroscedasticity, serial correlation and normality of residuals) were conducted. No assumption was violated and hence analysis was conducted as planned.

4. Findings and Discussion

4.1 Descriptive Statistics

The results in Table 1 provide the panel data descriptive statistics of the study variables.

Table 1: Descriptive Statistics

Variable		Mean	Std. Dev.	Min	Max	Observations
GDPg	overall	4.925229	3.661756	-9.523244	22.17389	N = 171
	between		.1000158	4.830443	5.029761	n = 3
	within		3.66084	-9.428458	22.18364	T = 57
Con	overall	22.41802	13.68545	4.67484	79.30172	N = 171
	between		3.253505	19.17564	25.68254	n = 3
	within		13.42361	3.058057	76.0372	T = 57
Comm	overall	2.024778	2.353159	.0486	10.85147	N = 171
	between		.1266647	1.879058	2.108513	n = 3
	within		2.350872	-.026315	10.99718	T = 57
Dom	overall	14.09731	9.442805	2.5	48.58	N = 171
	between		5.043443	8.435088	18.10772	n = 3
	within		8.491717	-.7204094	44.56959	T = 57

The findings in Table 1 show that the Real GDP Growth rate (GDPg) averaged 4.925% for the 57 years for the three countries. The standard deviation was high (Std deviation = 3.662) indicating that there was a high dispersion from the mean for the GDP growth rate. This is indicated by the range of the GDP growth rate that was from minimum (-9.523%) to maximum (22.17%). The ratio of concessional debt to

GDP (Con) averaged 22.42% for the three countries over the 57 years. The standard deviation was high (Std deviation = 13.69%). This was supported by the findings on the range (4.675% - 79.30%) which showed that there was high disparity amongst the levels of concessional debt to GDP amongst the three countries over the 57 years. On commercial debt (Comm), the study results show that the average commercial external debt to GDP ratio was 2.025% in the 57 years for the three countries. The standard deviation was high (std deviation = 2.353) indicating that there was a high dispersion of commercial external debt in the study period for the three countries. This is supported by the high range (0.0486 – 10.85) of the ratio of commercial external debt to GDP. Further, the results on domestic public debt indicate that the average domestic debt to GDP ratio was 14.1% with a standard deviation of 9.443. This indicates a higher dispersion over the study period for the three countries.

4.2 Fixed Effects Model

The study findings of the fixed effects panel regression model are provided in Table 2.

Table 2: Fitted Model on Effect of Public Debt on Economic Growth

Fixed-effects (within) regression		Number of obs	=	171		
Group variable: Country		Number of groups	=	3		
R-sq: within	= 0.1413	Obs per group: min	=	57		
between	= 0.3735	avg	=	57.0		
overall	= 0.0898	max	=	57		
		F(3,165)	=	9.05		
corr(u _i , Xb)	= -0.6315	Prob > F	=	0.0000		
GDPg	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]	
Dom	-.2562609	.0526805	-4.86	0.000	-.3602757	-.1522461
Con	.1151267	.0311495	3.70	0.000	.0536238	.1766297
Comm	.345792	.0951744	3.63	0.000	.1578753	.5337086
_cons	5.197029	.538385	9.65	0.000	4.134017	6.26004
sigma_u	1.3139898					
sigma_e	3.4434173					
rho	.12710603	(fraction of variance due to u _i)				
F test that all u _i =0:		F(2, 165) =	4.50	Prob > F = 0.0125		

The study findings presented in Table 2 establish that the model was statistically significant and a good fit ($F = 9.05$; $p < 0.05$). Besides, the study results indicate that the model explained 14.13% of the variation within the 57 years included in the study (r squared within = 0.1413). Moreover, the results show that the model explained 37.35% of the variation between the three countries (r squared between = 0.3735). Additionally, the results indicate that if POLS model was applied, the model could have explained 8.98% of the variation in GDP growth rate (r squared overall = 0.0898). Furthermore, the findings indicate that the model errors had a negative relationship with the independent variables ($\text{corr}[u_i, x_i] = -0.6315$). These results indicate that the error term had a negative moderate association with the regressors.

The findings in Table 4.6 indicate that concessional debt had a significant positive effect on economic growth ($\beta = 0.1151$, $t = 3.70$, $p < 0.05$). These findings suggest that concessional debt was important for economic growth for the three East African countries. Additionally, the results imply that a 1% increase in the ratio of concessional debt to GDP would increase the economic growth rate by 0.1151%. These findings led to the rejection of the first null hypothesis of the study which was;

H₀₁: External concessional public debt has no significant effect on the economic growth of three east Africa countries. The alternate hypothesis was therefore accepted.

The findings presented in Table 2 further established that commercial external debt had a significant positive effect on economic growth ($\beta = 0.3458$, $t = 3.63$, $p < 0.05$). These findings imply that an increase in external commercial debt was important in stimulating economic growth in the three East African Countries. The findings further showed that a 1% increase in the ratio of commercial external debt to GDP would result in an increase of 0.3458% in economic growth. These study findings led to the rejection of the second study hypothesis which was;

H₀₂: External commercial public debt has no significant effect on the economic growth of three east Africa countries. The alternate was hence accepted.

Regarding the effect of domestic debt, the study findings presented in Table 7 show that domestic borrowing had a significant negative effect on economic growth ($\beta = -0.2563$, $t = -4.86$, $p < 0.05$). These findings imply that an increase in domestic debt was detrimental to economic growth. The findings further show that a 1% increase in the ratio of domestic debt to GDP would result in a reduction in the GDP growth rate by 0.2563%. The study results led to the rejection of the third hypothesis of the study which was;

H₀₃: Domestic debt has no significant effect on the economic growth of three east Africa countries. The rejection of the null hypothesis meant that the alternate hypothesis was accepted.

4.3 Discussion of Findings

The study findings established a significant positive effect of external concessional debt on the economic growth of the three East African Countries. These findings imply that external concessional debt was important for economic growth for the three East African countries. These findings support the main propositions of the Keynesian theory that was developed by Keynes (1936), that there is no real burden associated with public debt and government involvement in economic activities. Besides, the study partially agrees with the findings by Casares (2015) that that concessional external debt can have a non-linear impact on a county's economic growth. When the indebtedness is high, an increase in the proportion of external debt to GDP hurts the economy. However, when the indebtedness is low, the increase in proportion promotes economic growth. The findings in this study imply that the concessional debt to GDP ratio for the three East African countries was not high enough to have a negative effect of economic growth. Furthermore, the study findings are supported by Kobey (2016) that the proportion of external concessional debt had a significant influence on the economic growth within the country.

The study findings, however, contradict some previous findings. For instance, the study results contradict the findings by Were (2001) which indicated that external concessional debt had a negative impact on the Kenyan economic growth. The contradictory findings could be due to the differences in the study contexts and the periods considered in the two studies. Additionally, the findings also disagree with the findings by Ejigayehu and Persson (2013) that external debt negatively influences the economic growth through debt crowding which relates to debt servicing. The findings from this study also contradict the findings by Senadza, Fiagbe, and Quartey (2017) that external debt has a negative impact on the economic growth of SSA states.

The study findings established that commercial external debt has a significant positive effect on the economic growth of East Africa countries. These findings support the debt overhang theory by Krugman (1988) which hypothesizes that at a certain level of debt to GDP, external debt has a positive effect on GDP but beyond this level, external debt repayment ability of the country falls below the contractual value of public debt which leads to burdening of the country. This makes the debt to have adverse effects on the economy. This view was also held by Cohen's (1993) theoretical model which established a non-linear effect of public borrowing on economic growth and investment. The study findings of the positive effect of commercial external debt, however, contradicts the results of various previous studies. For instance, the findings contradict the results by Kamundia (2016) who determined that commercial external debt has higher interest rates which increase the level of indebtedness for emerging economies. He further indicated that the primary debt burden for developing and underdeveloped states lie on commercial debts that are incurred at high annual interest charges. The high demands of commercial external borrowing increase the interest rates thus negatively affecting economic

growth. Besides, the findings were supported by Matiti (2013) who indicated that small economies engage in increased commercial borrowing after they exhaust concessional finance. The high-interest rates on commercial external debt enhance the cost of financing projects and private investments thus limiting economic growth. This was contrary to the effect of external commercial debt that was established in the current study.

On domestic borrowing, the study findings determined that domestic borrowing had a significant negative effect on economic growth. The implications of these findings are that increase in domestic debt was detrimental to economic growth. These findings support the crowding out the theory by Bacon and Eltis (1976) whose proposition is that increased government involvement in the financial and market economy adversely affects the remainder of the market. The findings of the negative effect of domestic borrowing on economic growth relate to findings from previous studies. For instance, the findings support the findings by Njoroge (2015) that the relationship between GDP growth and domestic debt is negative. Besides, the findings support the results by Ebi, Abu, and Clement (2013) that domestic debt have an adverse effect on the country's ability to grow economically.

5. Conclusions and Recommendations

The study concludes that external concessional debt is essential for the economic growth of the East Africa countries of Uganda, Tanzania and Kenya. Regarding external commercial debt, the study concludes that this form of debt is critical for the economic growth of the three east African countries. However, on domestic borrowing in the three East African countries, the study concludes that this is harmful to the economic growth of the three countries. Based on these findings, the study has implications and therefore, several recommendations are made for policy and practice.

First, the study recommends that the three East African countries should source for more external concessional debt through bilateral or multilateral arrangements to plug into their budget deficits, invest in strategic assets and finance projects in neglected sectors. This is expected to drive the economic growth of the different sectors while managing market imperfections. However, effective debt management should be observed to ensure that any external funds are applied prudently. Regarding external commercial debt, the study recommends that the three east African countries should consider this source of funding but ensure that a balance is struck between the different external financing sources. This will ensure that this source does not take a big portion of external funding since it is more expensive than other sources, such as concessional debt. Lastly, the study recommends that the level of domestic borrowing in the three East African countries should be reduced. This is because domestic borrowing is harmful to the economic growth of the three countries. Besides, the three governments should consider

other approaches to financing government spending but should not compete with the private sector in the financial markets for limited resources.

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