MAKERERE UNIVERSITY

IMPACT OF PUBLIC DEBT ON INVESTMENT AND ECONOMIC GROWTH: A CASE STUDY OF UGANDA

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ABSTRACT

The study empirically analysed the impact of public debt on investment and economic growth in Uganda for a period of 1980-2016. Two decades ago, Uganda's debt had peaked to unsustainable levels such that the economy did not have the capacity to meet its debt obligations. Fortunately, Uganda became the first country to qualify for debt relief under the Heavily Indebted Poor Country (HIPC) Initiative in 1998 and subsequently the Multilateral Debt Relief Initiatives (MDRI) in 2006. Again in 2017, Uganda downgraded from low to moderate risk of debt distress. This study sought to answer the question of whether Uganda's level and the trajectory of public debt are good for investment and economic growth. The study adopted simultaneous equation model to explore the direct, indirect and full effects of indebtedness on economic growth and the three-stage least squares (3SLS) method was used to estimate the systems of simultaneous equations.

The study revealed that public debt has been one of the obstacles to economic growth over the past thirty-six years in Uganda. The empirical findings revealed that public debt does affect growth negatively both directly and indirectly through investment channel. The results also indicate that debt service affects investment negatively; indicating public debt in in Uganda discourages investment rather than increasing it. From the result above it is possible to conclude that there is a sign of the debt overhang and crowding out effect on Uganda, and that Uganda's debt was not channelled to positively affect investment and hence economic growth. Uganda should reconsider its debt management policy, public investment management systems and investment options, if debt is important for growth as postulated in the theory. Uganda should reconsider its domestic and external borrowing questions of when and what to borrow for?