MAKERERE UNIVERSITY

EFFECT OF GOVERNMENT BORROWING ON ECONOMIC GROWTH IN UGANDA

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A RESEARCH REPORT SUBMITTED TO THE DIRECTORATE OF RESEARCH AND GRADUATE TRAINING IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF ECONOMIC POLICY MANAGEMENT AT MAKERERE UNIVERSITY.

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DECLARATION

I, Ayikoru Happy Gorrety, hereby declare that this research report titled "**Effect of Government Borrowing on Economic Growth in Uganda**," is my original work and has not been submitted to any institution of higher learning for any award.

Signed .....

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Date 08/01/2026.....

APPROVAL

This is to certify that the report of Ayikoru Happy Gorrety titled "*Effect of government borrowing on economic growth in Uganda*" has been submitted for examination with my approval as the University Supervisor.

Signed .....

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DEDICATION

Foremost, I want to offer this endeavour to the Almighty God for the strength, knowledge, peace of mind and good health he has provided during this research.

To my loving parents, Adaruku Cosmas and Eyako Eunice who have sacrificed so much for me to achieve my dreams. I hope this success is the reward you deserve. You made this possible. I love you mummy and daddy.

To Kugonza Michael, thank you so much for you unwavering support throughout this entire research journey. From early morning to late night discussions, your encouragement during moments of self - doubt and invaluable friendship have been the light guiding my path. Your belief in me made all the difference and for that, I am eternally grateful.

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LIST OF ACRONMYS/ABBREVIATIONS

HIPC – Heavily Indebted Poor Countries

PEAP – Poverty Eradication Action Plan

NPA – National Planning Authority

GDP – Gross Domestic Product

BOU – Bank of Uganda

NDP – National Development Plan

FY – Fiscal Year

USD – United States Dollar

IMF – International Monetary Fund

UGX – Ugandan Shillings

MDRI – Multilateral Debt Relief Initiative

EAC – East African Community

ARDL – Auto Regressive Distributed Lag

MoFPED – Ministry of Finance, Planning and Economic Development

REH – Ricardian Equivalence Hypothesis

CPI – Consumer Price Index

Std. – Standard

VIF – Variance Inflation Factor

SBIC – Schwartz Bayesian Information Criterion

AIC – Akaike Information Criterion

HQIC – Hannan Quinn Information Criterion

ECM – Error Correction Model

OLS – Ordinary Least Squares

GFCF – Gross Fixed Capital Formation

GGCE – General Government Consumption Expenditure

ABSTRACT

The nexus between public debt accumulation and economic growth remains pivotal yet a contentious issue within development economics, particularly for low-income countries navigating the dual imperatives of infrastructure-led development and fiscal sustainability. For nations like Uganda, where post-HIPC debt relief was replaced by a renewed and rapid accumulation of public debt to finance ambitious national development agendas, understanding the precise growth implications of this fiscal strategy is not merely an academic exercise but a matter of urgent macroeconomic policy. Escalating debt-to-GDP ratios and the associated rise in debt servicing costs threaten to compress fiscal space, crowd out productive investment, and potentially undermine the long-term growth prospects they intended to secure. This study, therefore addresses a critical empirical gap by providing a contemporary, rigorous analysis of how Uganda's specific debt trajectory shaped by strategic borrowing for Vision 2040 projects has influenced its economic growth from the post-relief era through to the present decade.

The primary aim of this research is to empirically examine the effect of government borrowing on Uganda's economic growth alongside other macroeconomic variables, distinguishing between short-run dynamics and long-run equilibrium relationships over the period 1994–2020. Moving beyond simple linear correlations, the study investigates the broader macroeconomic conditions in mediating the debt-growth relationship. This investigation is vital for policymakers at the Ministry of Finance, Planning and Economic Development and the Bank of Uganda, as it provides an evidence-based foundation for calibrating debt sustainability frameworks, optimizing the composition of public expenditure, and ensuring that borrowing genuinely catalyzes development rather than precipitating a costly debt overhang. Methodologically, the study employs an Auto-Regressive Distributed Lag (ARDL) bounds testing approach to cointegration, a robust technique suitable for analysing time-series data with a mix of stationary and non-stationary variables. Utilizing annual secondary data from the World Bank and Ugandan national sources, the model specifies economic growth (real GDP growth rate) as a function of total debt service, inflation, gross fixed capital formation, general government final consumption expenditure, and trade openness. Pre-and post-estimation diagnostics, including Variance Inflation Factor (VIF), Breusch-Pagan, and Jarque-Bera tests, confirm the model's validity, ensuring the reliability of inferences drawn. The most salient finding is the statistically significant negative long-run impact of general government final consumption expenditure on economic growth. This result provides empirical validation for neoclassical and debt overhang theories, suggesting that borrowed funds channelled into recurrent, consumptive spending crowd out productive private investment and fail to enhance the economy's productive capacity, thereby imposing a future growth penalty. Conversely, trade openness exhibits a positive and significant short-run effect on growth, highlighting the role of external sector vitality. While the direct coefficient on total debt service in the long-run ARDL model is marginally significant and negative, the more critical

mechanism is captured indirectly through the negative effect of government consumption. The Error Correction Term (ECT) of -0.421 is highly significant, indicating a moderate speed of adjustment approximately 42.1% of any disequilibrium caused by external shocks is corrected within one year as the economy reverts to its long-run growth path. The main takeaway from this study is that for Uganda, the composition and productivity of public expenditure financed by debt are more consequential for growth than the sheer volume of borrowing itself. The empirical evidence challenges the assumption that debt-financed public spending is inherently growth enhancing. Instead, it reveals that when borrowing primarily funds recurrent consumption, it acts as a drag on long-term prosperity, validating concerns of a latent burden of debt

CHAPTER ONE

INTRODUCTION

1.0 Introduction

Public borrowing has assumed great importance in recent years as indicated by the phenomenal rise in the volume of domestic as well as external debt. This is especially true in most of the countries, which belong to the group of poor developing countries of the world. There is a growing literature on the solution to the crisis supposedly faced by the world financial system because of these debts, some of which are considered to be unrepayable (Siddiqi, 2018). In many cases, the borrower may regard borrowing as an act of necessity rather than choice. However, according to the criteria used in economic analysis, any act of borrowing represents a choice since there is always an alternative, however unpleasant. Like private sector borrowing, government borrowing has a very long history heavily shaped by external forces like colonialism, which created a debt-cycle that many nations are still navigating today. The utilization of public debt is a fundamental instrument of fiscal policy, enabling governments to bridge the gap between recurrent and development expenditures and revenue collections. For capital-scarce developing economies like Uganda, borrowing is often justified by neoclassical growth theory, which posits that such financing is essential for augmenting capital accumulation, closing the infrastructure deficit, and elevating the steady-state level of output per capita (Madow, 2021). Consequently, public debt can be a critical catalyst for financing public investments in infrastructure, education and health thereby stimulating aggregate demand and fostering faster economic growth in the short-run.

However, the persistent accumulation of public debt beyond sustainable thresholds increases the burden and in turn, a drag on long-term economic prosperity. Theoretical and empirical literature consistently points to a negative debt-growth relationship in the long run, primarily through the mechanism of crowding out private investment. This occurs as government borrowing drives up domestic interest rates, increases expectations of future distortionary taxation, and can lead to inflationary pressures (Phiri, 2019). The consequence, as articulated by (Dedak, 2019) is the "burden of public debt," where each generation gives a smaller aggregate stock of capital to the next, leading to diminished output, lower consumption, and reduced economic welfare. This is particularly acute in countries with shallow financial markets, where domestic debt service can consume a significant portion of government revenues, thereby constricting the fiscal space for productive expenditures (Joy, 2020). Following the Heavily Indebted Poor Countries (HIPC) Initiative debt relief in the late 1990s and early 2000s, which significantly reduced the country's external debt burden, Uganda embarked on a renewed path of borrowing to finance its development agenda, notably outlined in frameworks like the Poverty Eradication Action Plan (PEAP) and subsequent National Development Plans (NDPs). This post-HIPC borrowing initially was directed towards rebuilding infrastructure and

stimulating growth. However, recent years have witnessed an alarming acceleration in the rate of debt accumulation. This escalating debt profile has been accompanied by a steep rise in debt servicing costs, which have become a central and contentious issue in Uganda's budgetary process. Much like the Ghanaian case, a critical indicator of distress for Uganda is necessarily its debt-to-GDP ratio, which, while rising, may still appear manageable in international comparison. (Kuria.M.W, 2022) further emphasizes that the composition of public expenditure, skewed towards recurrent spending at the expense of development expenditure, exacerbates this problem, limiting the productive capacity of borrowed funds. Despite significant borrowing, challenges such as stunted GDP growth per capita, high youth unemployment, and persistent poverty levels remain starkly evident. The National Planning Authority (NPA) has repeatedly raised flags over the sustainability of the current debt path, warning of potential debt distress (NPA, 2020). This fiscal strain compounded by vulnerabilities such as low domestic revenue mobilization, evidenced by a stagnant tax-to-GDP ratio, and exposure to external shocks, including fluctuating commodity prices and the global economic ramifications of events like the COVID-19 pandemic (IMF, 2024).

The central uncertainty prompting this research is whether Uganda's escalating public debt profile has been a stimulus for economic growth or a burden around the economy's neck. While previous studies have explored aspects of this relationship, the rapidly evolving fiscal landscape necessitates a fresh investigation using a more robust dataset and advanced econometric techniques to disentangle the short-run impulses from the long-run effects. This thesis comprehensively examines the impact of public debt on economic growth in Uganda, specifically determining the distinct effects in both the short- and long-run periods (1994-2020).

1.1 Background of the study

The eighth goal of the United Nations sustainable Development Goals requires member states to achieve an all-encompassing and workable economic growth as well as secure, productive and decent work for all by 2030 (UN, 2018). Member states of the UN have been struggling to meet this, making them to have very huge budget deficits since most of these countries cannot raise adequate capital from taxation by governments alone, for such investment (Erick, 2023). Most third world countries do not have enough savings for investments since most of these investments are capital intensive and dictate that countries have high savings that would contribute to the capital stock. When the government decides to borrow instead of introducing additional tax measures, to finance the budget deficit, it creates a liability on itself known as public debt. Although borrowing may appear attractive in the face of budgetary pressures and an increased number of crises in a changing global order, the study argues that borrowing to fulfil global responsibilities is generally morally problematic. Firstly, it

violates the "Just borrowing Principle"[1] and secondly, it demonstrates lack of sufficient commitment violating "Taking a stand Principle"[2] and therefore weakens. Public debt has become a major drain on transfer of external resources from African countries and majority experience large negative transfers, and it has been argued that large debt service payments made by indebted less developed countries retard their growth (WorldBank, 1989)

Government borrowing becomes necessary when government revenue sources are inadequate to finance growing government expenditures. The Nigerian economy has witnessed poor revenue growth because of over-dependence on volatile oil revenue and low tax capacity (Yusuf, 2021). This makes it one of the countries in Sub-Saharan Africa with stunted growth and dwindling income per capita and increasing poverty levels. Uganda like many other developing countries has a long history of borrowing from both multilateral and bilateral countries. Due to a combination of factors, including low domestic revenue mobilization, this narrow export base creates foreign exchange shortages, and the pressing need to finance large-scale public infrastructure projects that are central to its national development strategy all within context of limited domestic savings. (UBOS, 2025) estimates trend growth over the period 1990-1999 at about 6.8% per year with all the sectors growing relatively fast. The high growth rate was partly explained by the recovery process where the country was growing from a low base. In light of past performance, the NDP strived to achieve the objective of sustaining high levels of growth whilst at the same time maintaining macroeconomic stability. According to the BOU Monetary policy statement, economic growth was projected between 6.0% and 6.5% for FY2025/26 strengthening the medium term with factors like easing geopolitical tensions, higher infrastructure investment, and improved business confidence to boost the growth. Whilst falling commodity price, global supply chain disruptions, tighter borrowing conditions and bad weather affecting agricultural output that could constrain this growth (WorldBank, World Bank Indicators, 2025). Currently, the provisional total public debt stock increased from USD 23.66billion in FY 2022/23 to USD 25.59billion in FY 2023/24. External debt increased from USD 14.24billion in FY 2022/23 to USD 14.63billion in FY 2023/24 while domestic debt also increased from USD 9.43billion to USD 10.96 billion over the same period. The preliminary estimates of GDP indicate that the Ugandan economy grew by 6.3% in the fiscal year 2024/25 up from growth of 6.1% recorded in FY 2023/24. In nominal terms, the size of the economy increased to Ugandan shillings 226.344 billion in FY 2024/25 from 203,708 billion in 2023/24. During the period of FY 2015/16, the GDP i.e. the total income that is earned through the production of goods and services in an economic territory was USD 5.19% to 6.14% in FY2023/24 (WorldBank, 2025). The poverty level though has been steadily

[1] This argues that for government borrowing to be morally justifiable, it must be the overall best option when considering consequences of alternative actions like increase in taxes or doing nothing.
[2] Focuses on the nature and sincerity of a government's actions like imposing sanctions to condemn another state's actions.

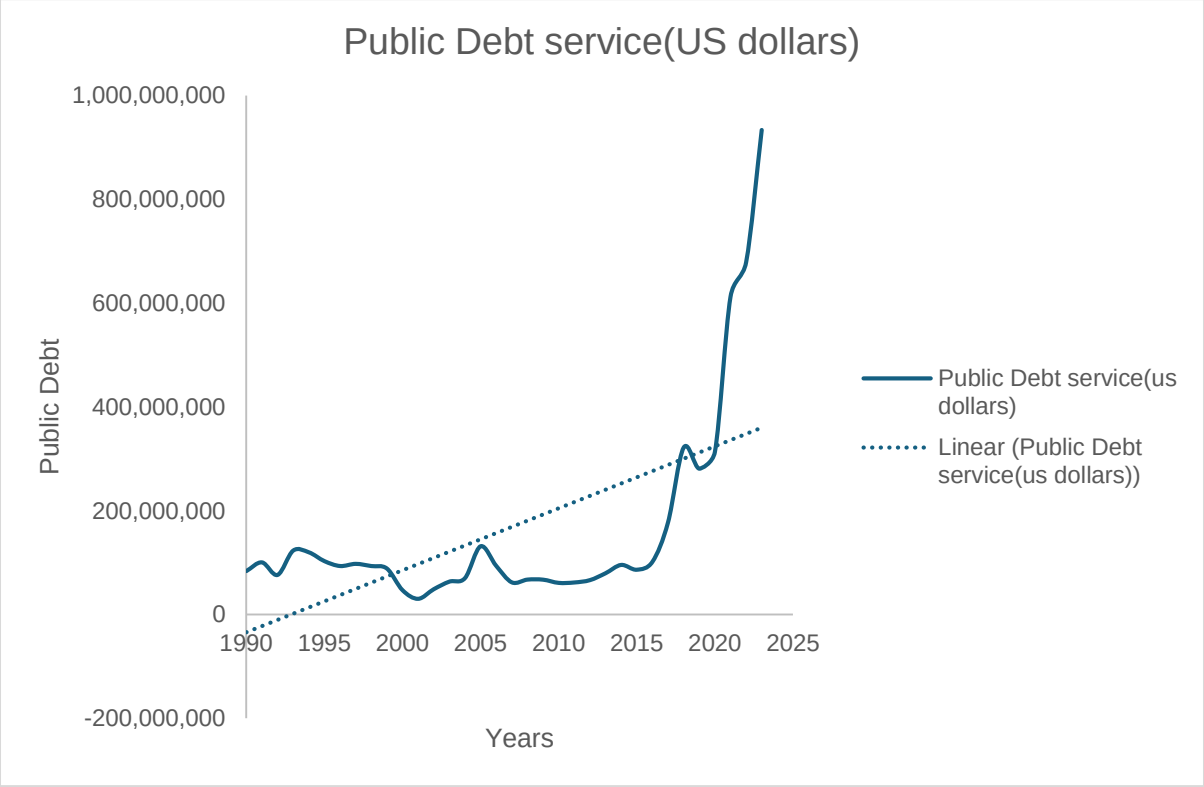
reducing over the years, it has remained significantly high in northern and eastern parts of the country (Oxfam, 2018).

Economic growth outlook is positive with real GDP growth estimated between 6.0% and 6.5% in FY24/25 and ascending beyond 7.0% in subsequent years (BOU, 2024). During the period 1981/82 to 2016/17, the debt sustainability of Uganda's public debt results shows that in the short run, government has been able to respond to past debt build up in a sustainable way (Bulime.W.N, 2019). However, in the long run, government has not been responsive to the debt bulge, which poses risks to debt sustainability. This can be seen in the NDPs where commitment to large-scale projects such as hydroelectric dams appear to overshadow immediate concerns about the escalating debt stock. This bulge is predominantly attributed to external borrowing for strategic infrastructure projects, including hydroelectric power dams and road networks. As a share of GDP, public debt reduced to 46.9 percent in June 2023 from 48.4 percent in June 2022. This reduction in the ratio of public debt to GDP was on account of a number of factors including, continued recovery in GDP growth within the economy expanding by 5.2 percent in FY 2022/23 compared to growth of 4.7 percent the previous financial year, appreciation of the end period exchange rate. Concurrently, the size of the economy doubled from UGX64 trillion in FY2010/11 to UGX128 trillion in FY2018/19 in nominal terms (NPA, 2020). While domestic revenue has improved over the years where collection increased from UGX5.02 trillion in FY2010/11 to UGX 16.359 trillion in FY2018/19 (NPA, 2020), it has constantly fallen short of targets failing to keep pace with the expanding expenditure needs. The escalating cost of debt servicing i.e. the interest payments associated with increase in the debt has become one of the items in the national budget that consumes a lot of resources that could otherwise be allocated for productive investments.

The economic literature presents a contradictory view of the relationship between public debt and economic growth. The traditional Keynesian economists advocate for a counter-cyclical fiscal policy, where increased government spending, even if debt financed can stimulate aggregate demand and pull the economy out of a recession (Barro, 1979). Conversely, the neoclassical view is that a debt financed government spending often leads to higher future taxes and interest rates which crowds out private investment and retarding long run growth. Within Uganda, the short-term symptoms of a potential debt overhang are already becoming visible. The national budget has increasingly been dominated by debt servicing obligations, for example, in the FY 2017/18, interest payments alone consumed 12.2% of the total national budget, a share that often exceeds allocations to vital social sectors like health and education. This fiscal pressure constrains the government's ability to invest in productive capacities and human development, potentially undermining the very growth objectives that the borrowing was meant to achieve. (Ssempala, 2020), provided a robust empirical analysis specific to Uganda, employing the ARDL bounds testing approach on data from 1980 to 2016. The findings confirmed a significant negative impact of public debt on economic growth in the short run,

attributing this to resources being diverted from productive uses to service debt. While the study suggested a potential positive long-run effect from the debt-to-GDP ratio if used productively it simultaneously highlighted a persistently negative impact from the total debt service to exports ratio, indicating an ongoing external sector vulnerability. There are persistent concerns, echoed in reports from institutions like the World Bank and the IMF, regarding project delays, cost overruns, and questions about the economic viability of some debt-financed mega-projects. If borrowed funds are not deployed with maximum efficiency and integrity, the debt incurred will not generate sufficient returns to justify its cost, inevitably leading to a negative net effect on economic growth.

Figure 1: Trend of public debt service (us dollars) for the period 1990-2023.



Source: World Bank.

The trajectory of Uganda's public debt service payments, as depicted in Figure 1 shows an upward trend. Following the significant debt relief under the HIPC initiative in the late 1990s and early 2000s, debt service obligations were low. However, the graph illustrates a pronounced and steady upward climb in these payments from the mid-2000s onwards. This trend aligns directly with the country's renewed borrowing for ambitious infrastructure projects under its National Development Plans and Vision 2040. The increasing slope indicates that a growing portion of national revenue is being diverted from productive public investment and social services to meet repayment obligations.

In conclusion, Uganda is attempting to strike balance between leveraging public debt as a necessary tool for financing its developmental ambitions and avoiding the severe economic stagnation associated with debt overhang.

1.2 Statement of the problem

The relationship between public debt and economic growth remains one of the most critically important subjects in development economics. Theoretical perspectives on this are divergent and lack convergence, leading to an empirical landscape filled with ambiguous and often contradictory findings. While classical (Smith, 1776) and neoclassical theories (Diamond, 1965) often posit a negative relationship due to crowding-out effects, future tax burdens, and reduced private investment, Keynesian and endogenous growth models suggest that debt-financed public expenditure, particularly in infrastructure and human capital, can be a catalyst for economic growth, especially in capital-scarce developing nations (Elmendorf, 1999). This theoretical difference is mirrored in empirical studies, where the effect of public debt on growth appears to be highly context-specific, dependent on factors such as the level of existing debt, the quality of institutions, the efficiency of public investment, and the macroeconomic environment.

Uganda's experience provides a distressing and inconsistent case study within this global debate. The country's modern economic history is deeply intertwined with the narrative of debt. In the 1990s and again in 2006, Uganda was a primary beneficiary of international debt relief initiatives, notably the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI). These programs, which provided substantial debt forgiveness, were designed to liberate the nation from unsustainable debt burdens and create fiscal space for growth-enhancing expenditures. Following this relief, Uganda's public debt stock was significantly reduced, falling to as low as US$1.6 billion, which was expected to pave the way for sustained economic development. However, this period of debt respite proved to be short-lived. Post 2006, Uganda embarked on an ambitious development path as outlined in its Vision 2040 and successive National Development Plans (NDPs), which prioritized massive investments in infrastructure such as roads, energy dams, and railways to transform the economy from a peasantry to a modern, middle-income status. A significant portion of the financing for these ambitious projects was sourced from both external and domestic borrowing. Consequently, the country's public debt stock has experienced a vivid and exponential resurgence. As documented by (Ssempala, 2020), the debt stock surged from UGX 14.257 trillion (US$5.5 billion) in 2000 to UGX 35.3 trillion (US$9.8 billion) by July 2017. This upward trajectory has continued, with the debt-to-GDP ratio surpassing 50% in recent years, raising alarms about debt sustainability. This rapid re-accumulation of debt, barely a decade after comprehensive forgiveness, presents a critical dilemma and a problem for policymakers whether this new borrowing is fuelling the intended economic transformation, or is it leading the country back into a debt trap that constrains growth?

The urgency of this question is amplified by emerging empirical evidence on the African continent, which suggests a non-linear and often detrimental relationship between high public debt and economic performance. For instance, a study by (Kuria.M.W, 2022) on EAC partner states like Kenya, Tanzania, Uganda, Rwanda, Burundi, South Sudan, found out that beyond a certain threshold, public debt begins to exert a significant drag on economic growth. The study identified that high debt servicing costs crowd out critical public spending on health and education, while also creating uncertainty that deters private investment. Similarly, (Moki, 2012), in an analysis of fiscal policy and growth in Sub-Saharan Africa, emphasized that the quality of public expenditure financed by debt is a decisive factor. When borrowed funds are channelled into consumption or inefficient projects with low social returns, the resulting debt accumulation fails to generate the necessary economic growth to service it, leading to negative feedback loops. This echoes the findings of (Cecchetti. G, 2011) and (Woo, 2010), who argue that high public debt levels impair growth through channels such as higher long-term interest rates, increased distortionary taxation, and elevated risks of economic crises. The period from 2017 to 2024 has been marked by continued aggressive borrowing to fund large-scale infrastructure projects, the economic disruptions of the COVID-19 pandemic, and global economic shocks that have increased borrowing costs and strained public finances worldwide. These recent developments render the existing empirical evidence incomplete. The core problem, therefore, is the lack of a comprehensive, up to date understanding of how this new and escalating wave of public debt is influencing Uganda's economic growth trajectory in the contemporary context. Has the short-run negative impact persisted or intensified? Is the hypothesized long-run positive effect materializing, or is the debt burden becoming a permanent drag on the economy? The optimistic view is that current borrowing is building the foundational infrastructure for future prosperity. The pessimistic view, supported by historical precedents and cross-country evidence, is that the country is on an unsustainable path that will compromise macroeconomic stability and long-term growth. Therefore, a critical investigation is required to determine the precise nature, and channels of the effect of Uganda's contemporary public debt dynamics on its economic growth from the post-relief era to the present day (1994-2020).

1.3 Research objectives

1.3.1 General objective

The broad objective of this study is to analyse the effect of government borrowing on economic growth in Uganda for the period 1994-2020.

1.3.2 Specific Objectives

1. To examine the trends and composition of Uganda's public debt composition (domestic and external) from 1994-2020.

2. To determine the nature and significance of the relationship between public borrowing and economic growth in Uganda, specifically testing for short-run dynamics and long-run equilibrium effects using robust econometric techniques.
3. To analyse the effects of macroeconomic variables that influence public borrowing and economic growth.

1.3.3 Research Questions

1. What is the nature of the relationship between government borrowing and economic growth in Uganda?
2. How do the macro-economic variables interact with government borrowing to influence Uganda’s economic growth trajectory.

1.4 Significance of the Study

The findings of this study are poised to hold profound significance for Uganda's socio-economic trajectory by providing an empirical anchor for critical national decisions. For policymakers within the Ministry of Finance, Planning and Economic Development (MOFED) and the Bank of Uganda, this research offers a vital evidence base to navigate the delicate trade-off between leveraging debt for accelerated development and avoiding the pitfalls of debt distress. The insights generated will directly inform the planning of Uganda's medium-term fiscal frameworks, guide the formulation of a sustainable debt management strategy, and aid in rectifying the optimal level and composition of public borrowing required to finance national ambitions like Vision 2040 without compromising long-term macroeconomic stability (MoFED, 2023).

The study carries substantial weight for the legislature, civil society, and the broader citizenry. It will equip Parliament with a robust, analytical foundation for its crucial oversight role, enabling more informed scrutiny of government loan approvals and budget allocations. For political leaders, the evidence clarifies the tangible consequences of public debt, enriching public debate and moving discourse beyond political to a fact-based discussion on fiscal responsibility. Furthermore, by elucidating the specific channels through which debt affects growth, this research empowers media, advocacy groups, and the public to engage more meaningfully on issues of national economic governance, fostering greater accountability and transparency. Finally, within the academic domain, this study makes a distinct contribution by providing a coarse, country-specific analysis of the debt-growth link in a dynamic, low-income country. It moves beyond broad cross-country panels to offer nuanced insights relevant to Uganda's unique economic structure and challenges, thereby serving as a valuable reference point and a springboard for further scholarly inquiry into the nation's fiscal policy and development economics.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter provides a comprehensive examination of the existing body of literature regarding the study on effect of government borrowing on economic growth. This review identifies significant divergence in empirical findings across developed and emerging economies, the theoretical framework necessary to investigate the specific conditions under which government borrowing transitions from fiscal stimulus to a burden of debt overhang and conceptual framework to discuss the relationship of the variables with growth.

2.1 Theoretical foundation

The theoretical literature on the relationship between borrowing and economic growth tends to be a negative relationship (Presbitero, 2010). Growth models augmented with public agents issuing debt to finance consumption or capital goods tend to exhibit a negative relationship between public debt and economic growth, particularly in a neo-classical setting, Keynesian model, Ricardian hypothesis and Monetarist view (Saint-Paul, 1992).

The Ricardian Equivalence hypothesis was constructed on the assumption that variations in public expenditures and revenues are matched by changes in private savings (Andres Kourtellos, 2013). The REH submits that regardless of the financing of public expenditures by debt or tax increase, the impact of the overall economic level on demand is identical (Ricardo, 1951)). The theory suggests that potential tax will allow debt repayment, that is, by the purchase of bonds issued by the government, individuals will boost their earnings (Barro, 1979)). The REH, further explains that when a government reduces current taxation and chooses to fund her budget deficits through issuing bonds, households do not increase consumption as they believe that the government would in future increase taxes so as to repay debts thus neither debts nor fiscal development has a lasting impact on economic growth (Afzal, 2012). (Donatus Onogbosele, 2016), in his line of argument, under certain settings the real economy is independent of the government's choice of raising revenue through either taxation or debt issuance.

In the view of the Keynesian economic theorists, the argument is that public debt withdraws cash from private investors, but then does not impact consumption because the borrowing funds are injected back into the economy to increase overall demand, perhaps, through wages and salaries and other capital expense (Donatus Onogbosele, 2016). Thus, Keynesian economic theorists ignored the challenge of financing budget deficits using either tax cuts or borrowing and emphasized frequent public interference to boost aggregate demand, jobs and production as fuelled by government borrowing, either domestically or externally (Udeh, 2016)

In the monetarist view, the expansion in government expenditures after a short time period, displace /crowd out a magnitude of private expenditures. Increasing government expenditure without any improvement in money supply increases production, profit and transaction demand for money (Ogunjimi, 2019). A constant money supply and increase in supply of debt in the market drive up interest rates. The rise in interest rates reduces business and government expenditure. The net result of the crowding out hypothesis is that the government sector growth tends to operate at the expense of the private sector, unless money supply rises during the process (Khan, 2001), this effect in the long run restricts the effectiveness of the government to influence the economy through fiscal policies.

The classical school of thought argues that public debt obstructs economic growth because it reduces both the financial discipline of the budget process and the private sector's access to credit in the economy (Broner, 2013). The theories and economic policies of classical economists do not only represent questions of historical but also of current interest, especially nowadays where the level and the structure of taxation, as well as the deficit and the public debt are high in the list of urgent problems requiring immediate action from governments (classical economists). In the neoclassical debt paradigm, there exists a positive relationship between debt and growth; this was based on the assumption of perfect movement of capital in terms of international exchange and deployment of resources from one country to another. Hence, the general assumption is that debt burden exists and weighs down economic growth through several channels related to debt stock and debt servicing. (Presbitero, 2010), after carefully supporting the neoclassicals, he suggests in his work that the adverse effects of debt services are due To Whom It May Concern. The crowding out of public investment, because the effect of debt service payment relies on net transfer from southern poor countries to feed expansion of northern or western countries, hence development of some countries at the expense of poverty.

The debt overhang theory suggests a new dimension to the growth-debt crisis and the basis of this theory is that if the level of a country's borrowing is over and above its capacity to pay, the expectation is that the debt servicing commitments will lead to a drain in the debtor's country output hence increasing the debt burden (Krugman, 1988). This theory purports that accumulation of debt will automatically lead to reduction in economic growth and tangle with development efforts through channels of reduced revenue and investment (Pattilo, 2002).

2.2 Empirical literature.

(Miller, 1961), considered that a situation in which the gross burden of national debt maybe offset in part or in total is when debt finances government expenditures that could contribute to real income of future generations. He further refined contributions by (Buchanan, 1958) & (Meade, 1958) by pointing out the impact of long-term interest rates, possibly in a non-linear form "if the government operation is of sizeable proportions, it may significantly drive-up interest rates since the reduction of

private capital will tend to increase its marginal product". He further stated that a situation in which the gross burden of national debt may be offset in part or in total is when debt finances government expenditure that could contribute to the real incomes of future generations, such as productive public capital formation. Two empirical studies specifically relate to nonlinear effects of debt (Pattilo, 2002), (Elbadawi, 1992) considers non-linear effects of debt on growth. They present fixed and random effect panel estimates of growth regression in which debt to GDP enters both linear and quadratic form. In addition, (Cohen D. , 1997) presents his method and does not use the debt stock directly in a growth regression but rather finds that a variable representing the predicted risk of a debt significantly lowers growth. He concludes that this method finds that debt ratios above which probability of rescheduling becomes excessive.

(Swamy, 2015), in his study of the indebtness of the government and what determines macroeconomics indicated that the rise in GDP, FDI, and inflation had unfavourable impression on indebtness. This test carried out using the panel granger model drew such a conclusion. (Diamond, 1965) added that the effect of taxes on the capital stock and differentiates between public external and internal debt. He concludes that, through the impact of taxes needed to finance the interest payments, both types of public debt reduce the available lifetime consumption of taxpayers, as well as their savings and thus the capital stock arising from the substitution of government debt, for physical capital in individual portfolios. (Christensen, 2007), in an IMF investigation of low-income countries, argues that well-developed domestic debt markets can support growth by improving financial intermediation and fiscal discipline. However, in countries with underdeveloped markets, excessive domestic borrowing may raise interest rates and crowd out private investment.

The flow effect of debt on economic performance usually crowding out public investments and consequently a larger debt service discourages public investments. It soaks up government budget resources and reduces money available for productive investments that encourage trade openness (William Easterly, 1993). (Akpan H, 1998), concludes that external debt burden has contributed significantly to a decline in investment in Nigeria. (Mukhopadhyay, 2002) constructed a disequilibrium framework to evaluate the relationship between this macroeconomic variables, his data is drawn from 9 developing countries and his results estimate reveals that rapid growth of external debt compressed private investment through their effects on both the demands for and supply of credit.

(Bevan, 2014) found that an increase in productive government expenditure, financed out of a rise in the tax rate, will be growth enhancing only if the level of domestic borrowing is sufficiently low according to a simple theoretical model integrating the government budget constraint and debt financing. Indeed, if higher public financing needs to push up debt yields, this may induce an increased net flow of funds out of the private sector into the public sector. This may lead to an

increase in private interest rates and a decrease in private spending growth by both households and firms (Elmendorf, 1999).

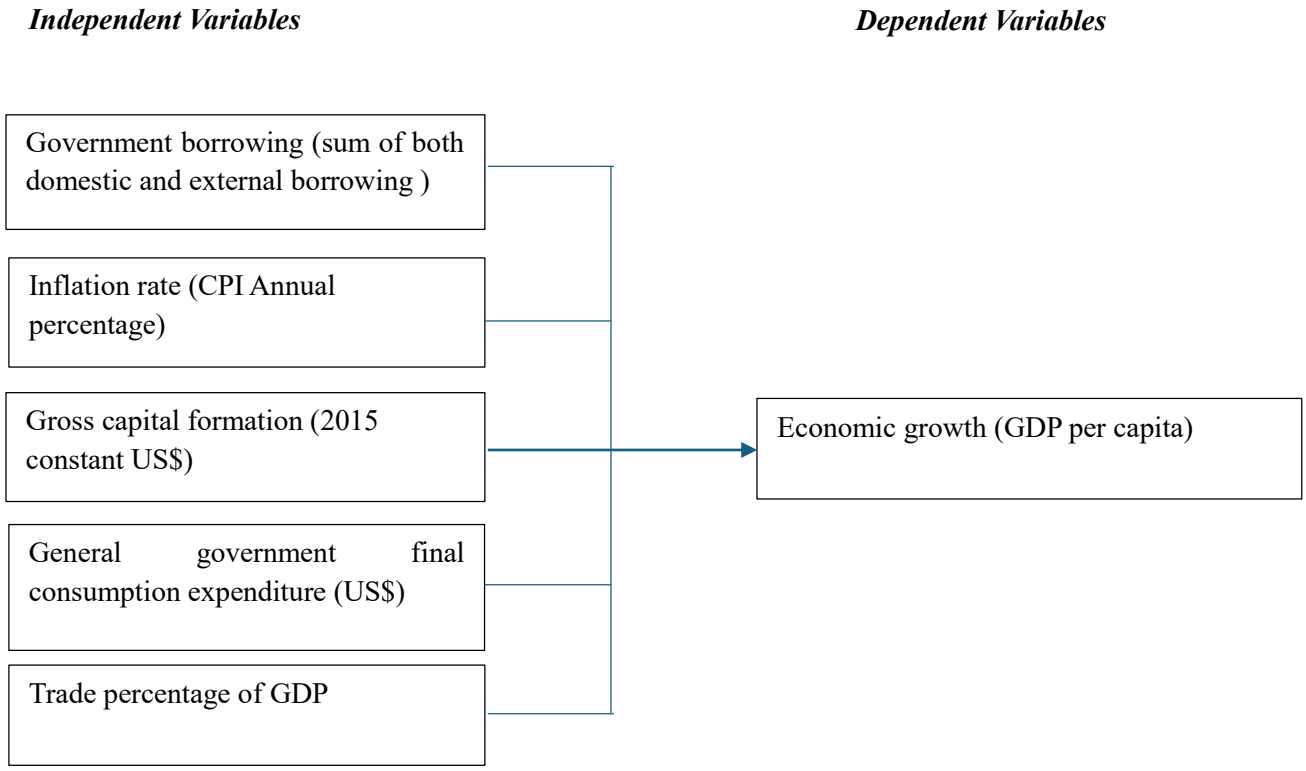
(Saint-Paul, 1992), considers a continuous-time overlapping generations, endogenous growth model based on (Blanchard.O, 1985) and concludes that an increase in the ratio of public debt to GDP reduces the growth rate of the economy. He further states that the reason for this relationship is monotonically negative is that an increase in public debt reduces a crowding out hindering economic growth. (Cecchetti. G, 2011) study shows that in cases of increased public debt, there is a high possibility of negative sustained economic growth and an unstable economic environment.

2.3 Conceptual framework.

Government borrowing (independent variable) can be broken into two frameworks that can be used to measure: domestic debt, which involves borrowing within the country through treasury bills and bonds held by commercial banks and local investors. External debt that involves borrowing from foreign sources like World Bank/IMF, bilateral partners like China. Strategic utilization of external resources can catalyse economic growth in developing countries by supplementing domestic resources and fostering development over time. This is particularly relevant for a country like Uganda, which has consistently faced substantial fiscal deficits driven by ambitious national development plans (such as the Vision 2040 framework) and infrastructural needs that outstrip domestic revenue mobilization. For Uganda, external borrowing is desirable when it finances productive public investment in areas like energy, transport, and agriculture, which are expected to yield an adequate rate of return. It can also help smoothen consumption and stabilize the economy against external shocks, such as fluctuations in commodity prices for its key exports like coffee. However, to avoid debt distress, the investments financed by this borrowing must achieve a real economic rate of return that is at least equal to the real interest rate on the debt. Since a significant portion of Uganda's borrowing is in foreign currency, this required rate of return must also be expressed in foreign currency (Iyoha, 1999). Uganda’s debt burden has historical roots, evolving from the post-independence era through periods of economic turmoil and subsequent structural adjustment programs. In recent years, the country has experienced a rapid accumulation of public debt, partly due to large-scale infrastructure projects and a reliance on non-concessional financing. This rising debt stock raises critical questions about its sustainability and its ultimate impact on Uganda's long-term economic growth prospects. The concept of external debt sustainability has, therefore, become an important issue in analysing Uganda's economic trajectory, balancing the need for development finance against the risks of future fiscal strain and potential debt burden. The change in debt levels over time is usually financed by borrowing. Economic growth (dependent variable) is defined as the total output produced by a country (Ssempala, 2020). In other words, it means an increase in the production capacity of the economy in terms of goods and services (Abbas, 2014) it occurs whenever people take resources and

rearrange them in ways that are more valuable. The government aspires to transform the economy from peasantry to middle-income status as indicated in NDP I and NDP II with optimal emphasis on infrastructure development in form of roads, electricity and innovations. This has prompted the government to commit many resources some of which have been solicited from foreign sources in the form of loans for such investments. At the current rate of borrowing, Uganda is likely to have detoriating economic growth partly because such borrowing adversely affects investments.

Figure 2: **Diagram showing conceptual framework**



CHAPTER THREE

METHODOLOGY AND DATA SOURCES

3.0 Introduction

This chapter presents the methodological framework employed to investigate the impact of government borrowing on economic growth in Uganda for the period of 1994 to 2020. The study adopted a quantitative research design, relying exclusively on secondary time series data. The primary tool for data compilation, organisation and preliminary analysis was Stata & Microsoft Excel.

3.1 Research design

The study adopted quantitative time series design using already existing data to provide empirical answers to the research problems. Econometric tests analysed the relationships between the variables to avoid spurious results in both short run and long run.

The design examined relationships between variables (public debt and economic growth) and analyses historical data to infer correlations and identify potential causal linkages based on economic theories.

3.2 Data types and sources

Secondary annual time series data for fiscal years FY 1994 to 2020 was obtained from World Bank, Ministry of Finance and Planning website. The study period was selected for the study because it captured transition from low debt in the mid-1990s to high-threshold scenarios of the 2010s, allowing for an empirical test of the non-linear relationship between borrowing and long -run growth. It is also difficult to manipulate data which is important for enhancing the validity and reliability of the study because data will be collected from existing sources (Ranganathan, 2019). In this case, it will be easier to evaluate what, where and how borrowing affects economic growth in Uganda thus establishing if there is a positive or negative relationship between study variables. However, there was no doubt envisaged about the reliability of the secondary data used, but the possibility of random errors has not been overlooked.

3.3 Data Analysis

The study utilized the Ms Excel tool pack and Stata, which plays a major role in aiding data analysis. Notably, the results of the descriptive statistics were provided where various indicators in the study were examined for determining significance of the research variables. The coefficient tests were used in showing whether independent variables have a positive or negative relationship and this helped to show if there is correlation between the variables. In addition, the R squared tests were conducted, which is a one indicator that helped in showing the percent of the model that can provide explanations for the variations in the context of the dependent variables and this can be utilized as a test of

significance in the study. Based on this, a regression model was used in data analysis where various variables of economic growth is regressed against economic growth. The model in multiple linear regression is as below,

$$\gamma = \alpha_0 + \beta_1\chi_1 + \beta_2\chi_2 + \beta_3\chi_3 + \beta_4\chi_4 + \beta_5\chi_5 + \varepsilon_t$$

Where,

γ= economic growth (GDP per capita)

α_0= constant term

χ_1= government borrowing (sum of both domestic and external borrowing in Uganda)

χ_2= inflation rate (CPI Annual %)

χ_3= gross capital formation (2015 constant US$)

χ_4=general government final consumption expenditure (US$)

χ_5=trade % of GDP

ε_t= stochastic error term

$\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ = partial coefficients of GDP in line with, $\chi_1, \chi_2, \chi_3, \chi_4, \chi_5$ respectively.

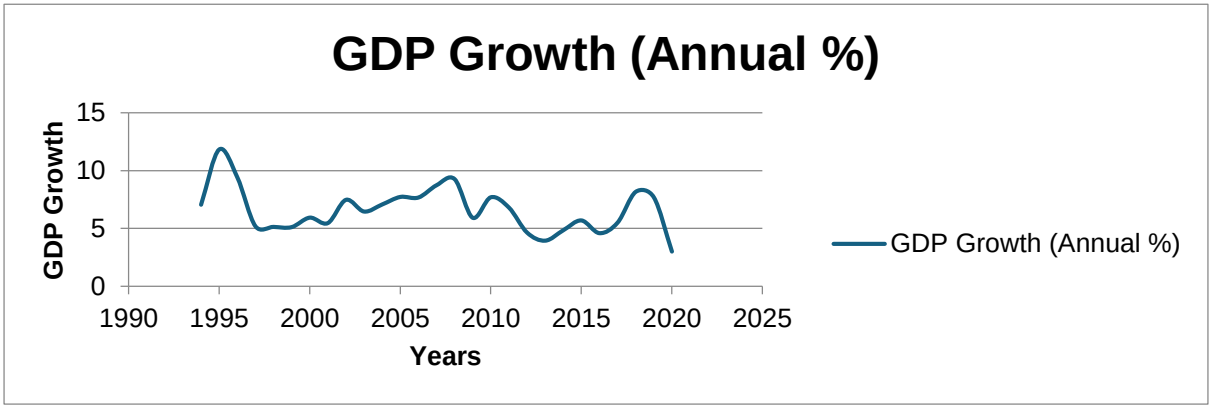
CHAPTER FOUR

PRESENTATION, INTERPRETATION, AND DISCUSSION OF RESULTS

4.0 Introduction

This chapter presents the empirical findings of the study on the impact of government borrowing on economic growth in Uganda. The analysis was based on the secondary annual time-series data covering the period 1994 to 2020. The chapter was structured to address the research objectives, beginning with descriptive statistics, followed by correlation and regression analyses to investigate the relationships between the variables and then econometric tests to ensure validity and reliability of the econometric model. The findings were then discussed in the context of existing economic theories and Uganda's specific situation. The chapter concludes with evidence-based policy recommendations derived from the analysis.

Figure 3: Trend of GDP Growth (Annual %)



Source:WorldBank

Figure 3, illustrates Uganda's real GDP growth from 1994 to 2020, highlighting a generally strong but unstable economic performance. The period was characterized by strong average growth, often exceeding 6%, which reflects successful post-conflict recovery and periods of significant economic expansion. However, the graph clearly highlights exposure to external and internal shocks, with noticeable dips corresponding to events like the global financial crisis around 2008-2009 and, most sharply, the COVID-19 pandemic in 2019/20. This volatility underscores the economy's underlying vulnerabilities, as discussed in the background. Despite substantial government borrowing aimed at stimulating and stabilizing growth, this disconnect suggests that while borrowing may have supported recovery from downturns, the borrowed funds have not consistently translated into higher, stable trend growth, pointing to potential inefficiencies in how debt is utilized to build economic resilience.

Figure 4: Trend of Total Debt Service (% of Exports)

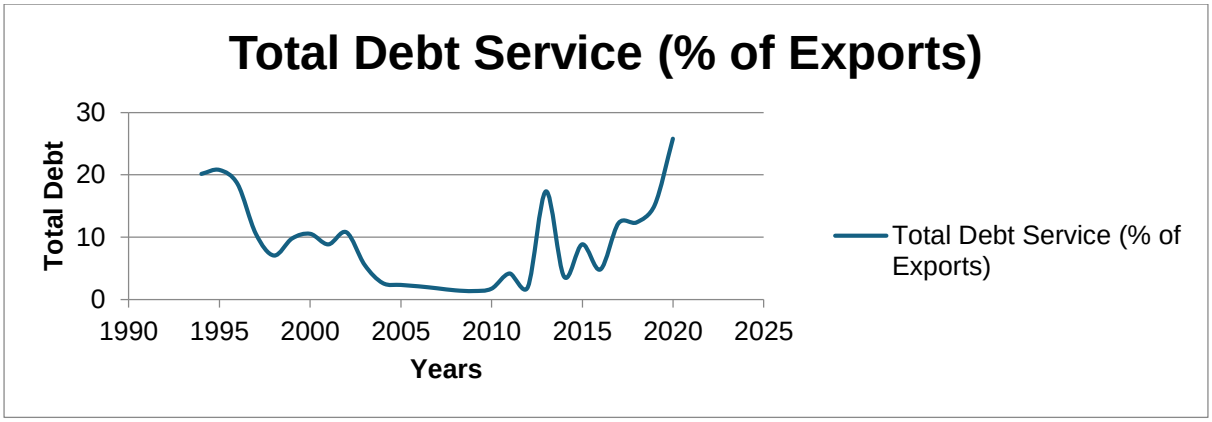


Figure 4, presents Uganda's total debt service as a percentage of its exports of goods and services. The trend shows significant fluctuation, with peaks indicating periods where a substantial share of the country's foreign exchange earnings was allocated to servicing external debt. High peaks, particularly in the later years of the series, are alarming. They demonstrate that even during periods of economic growth, the external debt burden creates a drain on foreign reserves, which directly affects the balance of payments. The figure provides empirical support for the debt overhang theory, where high debt service obligations can act as a disincentive for new investment and constrain the economy's capacity to generate the very growth needed to manage its debt stock sustainably.

4.1 Descriptive Statistics

The descriptive statistics were calculated to summarize the central tendency and identify potential outliers for robust econometric modelling (Moore.D., 2012) for the variables i.e. Economic Growth (Real GDP %), Total Public Debt Service (% of exports), and Inflation Rate (CPI Annual %), General government final consumption expenditure, gross capital formation, trade % of GDP.

Table 1: Descriptive statistics results for study variables.

Variable	Number of Observations (N)	Mean	Standard Deviation	Minimum	Maximum
GDP Growth (Annual %)	27	6.60	1.93	3.01	11.83
Total Debt Service (% of Exports)	27	8.99	6.97	1.36	25.82
Inflation (CPI Annual %)	27	6.25	4.04	-0.29	16.56
GFCF(US$)	27	10,298,848,816	20,366,860,855	1,347,039,140	91,399,444,139
GGCE (US$)	27	2,093,130,163	924,101,405.7	943,764,712.1	4,382,939,303
Trade % of GDP	27	37.94	5.91	27.83	56.26

The results in table 1, show a mean debt service ratio of 8.99% indicating that, on average, a substantial portion of Uganda's export earnings was allocated to servicing public debt. The median (8.85%) being very close to the mean suggests a relatively balanced central distribution for much of the period. This explains the escalating debt burden in the latter period of the study.

The inflation rate of 6.25% is above the typical central bank rate target of 5% (BOU, 2024) (WorldBank, World Development Report. Financial Systems and Development, 1989), indicating persistent underlying inflationary pressures with a standard deviation of 4.04%. The statistics for Inflation show an economy that has struggled with price instability, though with signs of improved management in more recent years.

The mean growth rate of 6.60% and a nearly identical median of 6.47% indicate a robust and consistent economic expansion over the period. This performance is strong by regional and global standards and indicates investment growth as well. However, this also underscores the economy's exposure to significant shocks, such as the global financial crisis, commodity price fluctuations, and the COVID-19 pandemic, which likely contributed to the lowest observed value in 2020. While gross capital formation (US$) grew with approximately 2.99% showed the economy experienced moderate growth. The general government expenditure of 2.09% represents a relatively low value and therefore indicated a conservative government spending or limited role of government in the economy. Trade % of GDP with 37.94 indicates a moderate level of trade openness suggesting the economy might somewhat be open and integrated into global markets and a more stable economy.

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4.2 Correlation Study

Correlation Statistics results for study variables

	GDP growth(% Annual)	Total Debt Service (% of exports)	Inflation(CPI)	GFCF(US$)	GGCE(US$)	Trade % of GDP
GDP Growth%	1					
Total debt service%	-0.157	1				
Inflation(CPI annual)	0.133	-0.288	1			
GFCF (US$)	-0.34	-0.03	0.039	1		
GGCE (US$)	-0.321	0.148	-0.67	0.413	1	
Trade % of GDP	0.168	-0.452	0.444	0.113	0.173	1

The results in table 2; show that there is a relationship between the variables and satisfy the second objective of the study. A Pearson correlation was to examine bivariate relationships (Pearson, 1895) between the variables and check for high-level multicollinearity between predictors (Cohen J. , 1988)

GDP Growth and Total Debt Service: The correlation coefficient indicates a very weak and negative relationship between public debt service and economic growth hence a unit change in the total debt service leads to a decrease in GDP growth by -0.0156. The negative correlation between debt and growth aligns with (Christensen, 2007) caution that in shallow financial markets like Uganda's domestic borrowing can quickly lead to crowding-out effects, raising the cost of capital for private firms.

GDP Growth and Inflation: The correlation coefficient is a very weak positive relationship. This shows that a unit change in inflation leads to a 0.133 increase in GDP growth.

Total Debt Service and Inflation: The correlation coefficient with a low negative relationship implies that a unit change in inflation leads to -0.288 decrease in total debt service.

Gross fixed capital formation and GDP growth: The correlation coefficient indicates that a unit change in the gross fixed capital formation leads to a -0.034 decrease in GDP growth. This is a very weak negative correlation.

General government final consumption expenditure and GDP growth: The correlation coefficient indicates that unit change in government consumption leads to a -0.321 decrease in GDP growth in the economy. This shows a weak negative correlation between the variables.

Trade % of GDP and GDP growth: the correlation coefficient implies that a unit change in trade leads to a 0.168 increase in GDP growth. This shows a very weak positive correlation between the variables.

4.3 Regression Results

Dependent Variable: GDP Growth (Annual %)

Table 3: **Regression results for study variables**

Variable	Coefficient	Std. Error	t-statistic	p-value
Total Debt Service	0.021	0.058	0.36	0.721
Inflation (CPI)	0.088	0.086	1.02	0.318
Trade % of GDP	0.076	0.079	0.96	0.347
Gross Capital Formation	-0.392	0.488	-0.80	0.430
Gov. Consumption	-1.182	0.452	-2.61	0.016
Constant	9.245	2.012	4.59	0.000

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Statistics:

R-squared	0.274
Adjusted R-squared	0.089
F-statistic (p-value)	1.48 (0.236)
Number of Observations	27

As presented in table 3, the P-values for the variables are (above the 0.5 threshold) and hence we conclude that we fail to reject the null hypothesis. The R-squared value is 0.274, meaning the model explains only 27.4% (which is very low) of the variation in Uganda's GDP growth.

The Adjusted R-squared is 0.089, which is a clear indicator that the model did not show a statistically significant relationship with the outcome due to omitted variables. The study utilized OLS regression to estimate parameters in the model (Wooldridge, 2016) provided the Gauss-Markov assumptions are satisfied (Gujarati, 2009)

In conclusion, the regression analysis provides limited statistical evidence that either Public Debt Service or other variables had a significant linear impact on Uganda's economic growth during the period 1994-2020. However, for every 1% increase in government consumption, GDP growth decreases by 1.18% often due to more spending on wages in developing countries rather than productive resources, which hindered growth, and a tax is required to fund it (Barro, 1979). This finding suggests that the drivers of Uganda GDP growth are more complex and were not captured in this model with these macroeconomic variables alone. Other factors not included in this model are likely the primary determinants of growth**.**

4.4 Variance Inflation Factors (VIF)

Table 4: Test for multicollinearity.

Variable	**VIF**	**1/VIF**
Government Consumption	1.24	0.806
Gross Capital Formation	1.22	0.820
Trade % of GDP	1.35	0.741
Inflation	1.32	0.758
Total Debt Service	1.28	0.781
Mean VIF	1.28	

High multicollinearity is problematic as it inflates the standard errors of the coefficient estimates, making it difficult to determine the individual effect of each predictor on the dependent variable. A VIF is carried out to test for multi collinearity (Marquardt, 1970) and table 4 indicates that values range from 1.22 to 1.35 with a mean VIF of 1.28. This confirms that multi-collinearity is not a

problem in this regression model. The estimated coefficients are stable (below threshold of 5) and their standard errors were not inflated by high correlations among the predictors (Hair JF, 1998)**.**

4.5 The Breusch-Pagan Test.

Table 5: Test for heteroscedasticity.

Test Statistic	**Value**	**Degrees of Freedom**	**p-value**
chi2	6.45	5	0.265

To ensure the reliability of the standard errors and the efficiency of the OLS estimators (Greene, 2012), the model was tested for heteroscedasticity using the Breusch-Pagan. This diagnostic is critical because the presence of non-constant error variance can lead to biased standard errors (Pagan.R.A, 1979). The test in table 5; yields a chi-square [$\chi 2$ (5) = 6.45] with a ρ =0.265 that is greater than the significance level of 0.05, we fail to reject the null hypothesis which shows the variance of the error term is constant. This means that there is no statistical evidence of heteroscedasticity in the regression model.

4.6 Jarque-Berra Test.

Table 6. Results for Normality test.

Test Statistic	**Value**	**p-value**	**Skewness**	**Kurtosis**
Jacque-Berra	3.15	0.207	-0.45	3.1

The Jarque-Berra test evaluates normality by examining the skewness (-0.45) and kurtosis (3.1) of the residuals (Jarque, 1987). As shown in table 6, the test yielded a statistic of 3.15 with a $\rho = 0.207$ that is significantly greater than the threshold significance level of 0.05 we fail to reject the null hypothesis. This shows that the residuals are normally distributed which is a prerequisite for validity in small sample econometric modelling (Brooks, 2019). When combined with the findings of the Breusch-Pagan test, these confirm that the model meets the Gauss-Markov assumptions for best linear unbiased estimators (BLUE) (Gujarati, 2009).

4.7 ARDL Test (Optimal Lag Selection)

Table 7: ARDL results

Lag	LL	LR	p-value	FPE	AIC	HQIC	SBIC
0	-150.23				11.71	11.81	12.01
1	-120.45	59.56	0.000	0.001	10.03	10.48	11.28*

2	-105.12	30.66	0.002	0.001	9.89*	10.69*	12.09

Table 8: Error Correction Model (ECM) results

Variable	**Coefficient**	**Std Error**	**t- statistic**	**p-value**
ECT(-1)	-0.421	0.152	-2.77	0.012**
ln Debt service	-0.085	0.047	-1.81	0.086*
ln inflation	0.032	0.038	0.84	0.411
ln trade	0.124	0.071	1.75	0.098*
ln GFCF	-0.156	0.089	-1.75	0.097*
ln GovCons	-0.238	0.102	-2.33	0.031**
Short-run dynamics(Δ)				
Δln Debt service (-1)	0.021	0.032	0.66	0.517
Δln Inflation(-1)	0.015	0.028	0.54	0.596
Δln Trade(-1)	0.089	0.041	2.17	0.043**
Δln GCF(-1)	-0.067	0.038	-1.76	0.095*
Δln GovCons(-1)	-0.092	0.045	-2.04	0.056*
R - squared			0.482	
Adj. R- squared			0.312	
F-statistic			2.83 (ρ = 0.024)	
DW- statistic			2.14	

Prior to estimating the long-run relationships, an optimal lag structure for the ARDL was determined to avoid serial correlation and to ensure the efficiency of the estimators and this was done after transforming the variables into their lag form to get more accurate variance results. The choice of ARDL follows the methodology of (Pesaran, 2001) because it allows estimation of cointegration relationships regardless of whether the underlying variables are integrated of order I(0) or I(1) hence more robust results. As shown in Table 7**,** SBIC at lag 1(11.28*), AIC reached its minimum at lag 2 (9.89*) which is preferred for its ability to capture more complex dynamics in macroeconomics data. The key finding is that there is a stable long-term relationship, much like connection of Uganda's debt levels and its economic growth. Debt service was not significant in the OLS and had a weak long run effect (8.5%) in the ARDL. Specifically, our calculations show the economy corrects about 42% each year. The significant negative long-run impact of government consumption aligns strongly with the Neoclassical and Debt Overhang theories (Krugman, 1988). Neoclassical theory suggests that debt-

financed government spending, particularly on consumption, crowds out private investment by raising interest rates and expectations of future taxes. A 1% rise in government consumption reduces growth by 0.24% in the long run empirically validates this crowding out effect, suggesting that borrowed funds used for recurrent expenditure do not enhance Uganda's productive capacity. The Durbin-Watson statistic of 2.14 indicates no evidence of first-order serial correlation in the residuals, confirming the assumption that the residuals are independent (Kenton, 2025).

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

The conclusion is that Uganda's post-HIPC public borrowing, in its current composition and application, has not served as a significant direct catalyst for economic growth. The findings resonate with the neoclassical warning of the "burden of public debt," not necessarily through the direct channel of debt service in this model, but through the indirect, yet significant, channel of potentially unproductive government consumption.

The findings present a policy relevant narrative for this research that is that the impact of public borrowing on Uganda's economic growth is not inherently positive or negative but is critically mediated by the composition and efficiency of the expenditure it finances. The analysis reveals a statistically significant negative long-run relationship between general government final consumption expenditure and GDP growth. This key finding empirically validates neoclassical and debt-overhang theoretical concerns, indicating that when borrowed funds are channelled into recurrent, consumptive spending, they fail to augment the economy's productive capacity and instead crowd out more productive private investment, thereby imposing a long-term drag on growth. In contrast, the study finds that trade openness provides a significant positive stimulus to the economy in the short run, underscoring the vital role of the external sector. The significant and correctly signed Error Correction Term (ECT) of -0.421 further confirms a stable long-run relationship among the variables, with the economy displaying a moderate speed of adjustment to shocks.

Therefore, the implication of this research is that Uganda's current challenge is not solely the level of its debt, but rather the quality of its debt-financed fiscal policy. The significant resources committed to debt servicing and recurrent consumption, as evidenced in the trends, risk constricting the fiscal space necessary for transformative public investment. While borrowing remains a necessary tool for a capital-scarce economy, this study demonstrates that its benefits are not automatic. For debt to be a force for sustainable development, it must be strategically deployed within a framework of sound fiscal governance, stringent investment appraisal, and an unwavering focus on productivity-enhancing expenditures. The path forward, as illuminated by this analysis, requires a decisive policy pivot to ensure that public debt builds the foundations for future prosperity rather than becoming a recurring constraint on Uganda's economic potential.

5.1 Policy Recommendations.

To transform public borrowing from a potential burden into a catalyst for sustainable growth, Uganda's fiscal policy must undergo a strategic reorientation based on the empirical findings of this study. Specifically, the significant negative long-run impact of government consumption necessitates

a binding shift in expenditure composition mandating that borrowed funds be strictly allocated to high-return capital investments in infrastructure and productive sectors rather than recurrent spending. Concurrently, the positive short-run stimulus from trade openness must be leveraged through aggressive export diversification and regional integration to generate the foreign exchange earnings required for sustainable debt service. Furthermore, to ensure these borrowed funds yield growth, institutional reforms are essential strengthening parliamentary oversight of loan approvals, implementing rigorous public investment management systems to curb inefficiency, and accelerating domestic revenue mobilization to reduce recurrent budget reliance on debt. This integrated approach prioritizing productive investment over consumption, harnessing trade, and enhancing fiscal governance is critical for Uganda to avoid debt overhang and achieve the transformative growth envisioned in its national development plans.

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