

## **Impact of Public Debt and Corruption on Economic Growth in Sri Lanka**

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### **Abstract**

Governments tend to borrow financial resources from domestic as well as external sectors when their tax revenues are not sufficient to meet the required financial needs. In the Sri Lankan context, there has been a gradual increase in the accumulation of public debt since the post-liberalization phase. Herein, this ambience of public debt has caused congenial effects while leading to some unfavorable effects on the economy. With that, there are many studies that look into the relationship between public debt and economic growth. It is hard to find, however, research addressing the role of corruption between these two variables in the Sri Lankan context. Noticing this vacancy in the current literature, this study strives to investigate the effect of public debt and corruption on economic growth in Sri Lanka over the period 1973–2022. The study used public debt and corruption as explanatory variables and investment, savings, debt service, and trade openness as control variables to determine their effect on GDP growth. The study follows some econometric steps, respectively, the unit root test, the Johansen co-integration test, and finally employing the Vector Auto Regression Model (VAR) to detect the short-run impact, on the one hand, between public debt and economic growth and, on the other hand, between corruption and economic growth. The results indicate that there is a negative relationship between public debt and economic growth reveal evidence for the presence of a crowding-in effect of public debt, implying a significant association between public debt and economic growth. In addition, the study's empirical results show that a negative relationship between corruption and economic growth also indicates that corruption hinders economic growth in Sri Lanka. The finding suggests that using government debt for priority investment expenditures with a prudent debt management strategy to curtail the impact of crowding out investment will have a favorable impact on the economic growth of the country, particularly in the long run. It also suggests that the issue of corruption be tackled head-on by strengthening anti-corruption laws, which should apply to high-level and low-level positions in the public sector. These findings are important for the government of each regional country to further manage the corruption in the country and for public service providers in their decision-making processes.

**Keywords:** Public Debt, Corruption, Economic Growth, Sri Lanka