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# EXPLAINING THE RELATIONSHIP BETWEEN PUBLIC EXPENDITURE AND ECONOMIC GROWTH IN KENYA USING VECTOR ERROR CORRECTION MODEL (VECM)

## Abstract:

The rapid growth in public expenditure in Kenya since independence has caused concern among policy makers on its implication on economic growth. The main aim of this study therefore was to explain the relationship between economic growth and public expenditure on Health, Education, Military and Infrastructure in Kenya. The study used a time series data collected between 1963 - 2012. Johansen Cointegration Test and Vector Error Correction Model (VECM) was applied on the time series data to estimate the short-run and long-run relationships between public expenditures and economic growth in Kenya. The results suggests that public expenditure components and economic growth co-move towards a long run equilibrium with a speed of adjustments of approximately 3.6% after short run fluctuations in the equilibrium. Furthermore, the results show no casual relationship between public expenditure and economic growth in Kenya. However, there exist a unidirectional causation between Military and Health expenditures - Military expenditures "Granger Cause" Health expenditures. Hence, a change in Military expenditures cause a change in Health expenditures. These findings suggests that the Government of Kenya switch military expenditures for health expenses in Kenya, but not vice versa.

## Keywords:

Vector Error Correction Model (VECM), Granger Causation, Public expenditures, Economic Growth, Kenya.

**JEL Classification:** H50, O47, O55

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