Deficit financing and Economic Growth: Evidence from Sub-Saharan African Countries

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Abstract: In view of the growing controversy on financing of budget deficits, this study investigates the implications of deficit financing in the Sub-Saharan African countries and how it has impacted on their growth rate. Specifically, it looked at how domestic debt, external debt, external reserves, and budget deficit affects real gross domestic product (RGDP). The study utilized panel data gotten from the statistics databank of the various Central Banks in the Sub-Saharan region and the development indicators of the World Bank for period 1986 - 2021; thus, giving a total observation of 144. The Hausman statistics gave the panel fixed effect regression technique as the most appropriate analytical method, which revealed short run relationship at the 5% significant level. From the result of the study, both external reserves and domestic debt are positive and significant to gross domestic product; external debt is negative and insignificant to gross domestic product; while budget deficit is negative and insignificant to gross domestic product. In conclusion, deficit financing affects the growth rate of most Sub-Saharan African economies. The study recommends among others that both fiscal and monetary agencies of the Sub-Saharan countries should maintain optimum level of domestic debt as it is one of the mechanisms for economic growth. Also, is the enforcement of economic policies to aid increase in external reserves.

Keywords: Expansion, Financial Institutions, Parsimonious Model, Interest rate.
JEL Classification: F34, F63, F65, G28, H62, H68, O55

1. INTRODUCTION

One of the economic issues confronting both developed and developing countries/economies is deficit finance. Since the late 1970s, Sub-Saharan Africa has experienced huge government deficits, which has sparked debate among policymakers and economists (Keho, 2016). Deficit finance refers to raising funds to meet the deficits caused by spending that exceed revenue. These shortfalls are plugged by borrowing from the public through bond sales, printing fresh money, or borrowing from outside sources. This means that deficit finance is a powerful weapon for promoting economic growth and development in countries around the world, particularly in growing economies like Nigeria, Kenya, Cameroon, and South Africa (Onuorah & Ogbonna, 2014). Clearly, deficit financing has aided in the correction of these countries’ budget imbalances over the years. Indeed, if a borrowing country uses deficit financing well, it will raise domestic savings and, in turn, economic development.

Basic preconditions or fundamentals for investments to occur include the achievement of specific macroeconomic goals including quick and sustained economic development, low inflation, a low and cheap foreign exchange rate, and balance of payments equilibrium. Regrettably, the majority of Sub-Saharan African nations are characterized by poor income, steadily rising inflation, and balance of payments imbalance, among other things. This is clear from the vast infrastructure gaps that are now present in the region, leading to a financing shortfall of 4% of GDP (IMF, 2019).

Coulibaly, Gandhi and Senbet (2019) assert that the historical development of the region demonstrates that many countries need major investment. This means that the region will have to close a financial gap that represents an...
average yearly GDP deficit of 12%. This is quite challenging to generate about $230 billion a year given the low rate of savings in the area. In order to raise the funds required for their own initiatives, many countries in the area have turned to external financing to address this enormous challenge. Therefore, the purpose of borrowing is to compensate for a shortage of domestic resources in order to hasten economic development and expansion (Labonte, 2012).

Deficit financing in any economy has consequences which could be advantageous or disadvantageous depending on its impact on economic activities. For instance, how fiscal policy prompts macroeconomic management was explained by the neo classical, Keynesian, and Ricardian schools of thought (Mashakada, 2013; Onwe, 2014). The classical school of thought, in particular, contends that government intervention in the open market is unnecessary because the economy will eventually adjust to a new equilibrium level after some volatile periods. It also contends that by increasing real rates of interest; along with driving away private investment, fiscal deficits tends to be insignificant to rate of growth of an economy (Onwe, 2014). The Keynesian school of thinking, on the other hand, acknowledges the necessity for government intervention to correct any possible economic instability that the market system is unable to address. The adoption of fiscal policy measures to attain full employment, which is the ultimate objective of macroeconomic policy, was sparked by the adoption of this ideology, particularly in the post-depression years. This has formed a new face in economic reasoning and policies (Nwaeke & Korgbeelo, 2016; Eze & Nwambeke, 2015; Onwe, 2014). According to the Ricardian equivalence theorem, deficit financing does not pose any direct significance on economic activities. Barro (1989) assert that, since higher public consumption necessitates higher taxes, any decrease in current-year taxes must be offset by an increase in the present value of future taxes, leaving both public consumption and interest rates unchanged. Considering what has been said thus far, it appears that different viewpoints have been expressed in the literature regarding the macroeconomic effects of budget deficits. This is because the existing nexus connecting macroeconomic variables like growth, unemployment, exchange rates, and inflation and budget deficits, may or may not necessarily be negative.

Debt crisis is a result of the uncontrollable accumulation of a lot of debt, which makes repayment difficult or impossible and leads to imbalances in the domestic and global political economy (Matuka & Asafo, 2018). The prime objective of this research is to empirically investigate the growth rate of sub-Saharan African nations by way of deficit financing particularly in relation to Kenya, Nigeria, South Africa, and Cameroon as well as its effect on the real sectors of manufacturing, production, mining, and other productive arms of the economy.

There is ongoing discussion about the effects of foreign debt and investment on growth as a result of many sub-Saharan African nations’ continued reliance on foreign debt to pay for their fiscal deficits (Adesuyi & Falowo, 2013). As a result, the section is currently facing an urgent financial issue. Taking total external equity as an example, it climbed from $213.4 billion in 2010 to $367.5 billion in 2013 (Ali, 2014). The overall government debt (as a percentage of GDP) increased from 23 percent in 2013 to 62 percent in 2016 (IMF’s Global Economic Outlook, 2017). Despite sizable borrowings by numerous sub-Saharan African nations, little has really not changed regarding investment in infrastructure and other crucial areas.

A handful of the arguments made by some experts seem to be a mirage and do not accurately reflect the present events in the Sub-Saharan Africa (Ibrahim, 2015). While scholars, like Nwanna and Umeh (2019), Solawon and Adekunle (2018), think that deficit financing has a substantial impact on the economy, other researchers, like Sulaiman and Azeez (2012) and Nwanne (2014), think that it has no significant impact. This still requires empirical research.

A careful review of the empirical literature in Olusegun et al., (2020); Omodero, Egbide, Madugba and Ehikioya (2020); Odubuasi, et al., (2018); Okah et al., (2019); Richard and Ogiji (2016); Osoro (2016); Elwasila and Mohamed (2018); Akinola (2017); Ugwu (2017); Monogbe, et al., (2015) shows that most of the studies made used of annual time series; however, this study is different as it utilized panel series for four Sub-Saharan African countries. Moreover, Ifeanyi and Umeh (2019), Omodero and Alpheaus (2019), Odubuasi et al., (2018), Okah et al., (2019), Richard and Ogiji (2016), Osoro (2016), Elwasila (2018), Fagbohun (2017), and Ugwu (2017) have focused on the use of three variables as a proxy for deficit financing, such as external debt, domestic debt, and foreign reserves. This study incorporates an additional component in its analysis - the budget deficit. This study contends that before any government may consider sourcing funds, either internally or externally, her budget must be in deficit, and the magnitude of the deficit is important to her sourcing for funds. Aside from that, African countries’ desire for economic expansion, particularly in Sub-Saharan Africa, requires running budget deficits in order to expand their economies. As a result, it is vital that this nexus be empirically explored in order to determine whether budget deficits actually benefit Sub-Saharan African countries, or the inevitability for deficit financing is viable in light of the divergent opinions around it.

In a bid to provide answer to this pressing issue, this study investigates deficit financing and its effect on the growth of the Sub-Saharan African countries during the period 1986 to 2021. The idea is to ascertain if deficit financing

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has promoted economic growth in these countries. In doing this, the study attempts to also identify the causal link between economic growth rate and deficit financing.

2. LITERATURE REVIEW

Keynesian Theory of Deficit Financing

Keynes' (1936) theories had a significant impact on the evolution of economic thought in the 20th century. A policy of active governmental intervention in the economy was implemented as a result of these concepts (Ahmad, 2019). This intervention made the state use a variety of methods for funding government spending, which led to a focus on deficit financing in particular (Monogbe & Okah, 2017; Olulu-Briggs & Onoh, 2014). According to Keynes, the government's job during an economic downturn is to borrow money and invest in the economy (Okoro, 2013). First, the greater the disparity between actual and potential productivity, and the more glaring flaws are in the economic system, and the richer the community. Second, because poor communities often consume the majority of their products, full employment can be achieved with very little investment. Third, for the savings tendencies of wealthy members to match the employment of poor members, wealthy communities must find many lucrative investment options. Therefore, Keynes emphasizes the importance of willingness to consume, marginal capital efficiency, and interest rate theory (Odi & Olulu-Briggs, 2018; Owoye & Onofowora, 2004; Okoro, 2013).

The Dual Gap theory of Deficit Financing

This idea is put forth with the understanding that the government must make significant investments in order to achieve the right degree of economic development. However, without significant domestic funds, such investments cannot be made constantly. This indicates that for a nation to develop at a rate that is sustainable, it needs to invest heavily and accumulate significant domestic savings (Ifeanyi & Umeh, 2019; Osuka & Achinihu, 2014; Olulu-Briggs & Odi, 2011). However, these domestic savings and investments are insufficient to accomplish comprehensive development, necessitating foreign borrowing of capital. This implies that, domestic savings, investment, and foreign borrowing are all functions of economic progress. In addition, if resources from outside are needed to supplement domestic ones, as in cases of excess import vs export, (i.e. M > E), then;

\[ I > S \text{ and } M > E \]

Hence, \[ I - S = M - E \]

In national income accounting, an excess of investment over domestic saving is equivalent to excess surplus of import over export.

\[ \text{Income} = \text{consumption} + \text{import} + \text{savings} \]
\[ \text{Output} = \text{consumption} + \text{export} + \text{investment} \]
\[ \text{Since Income} = \text{output}, \text{then Investment} - \text{Saving} = \text{Import} - \text{Export} \]

Omoruyi (2005) discovered that most economies relied on foreign borrowing to close the gap between savings and investment levels. This gap serves as justification for external debt which is sook to make up for the lack of savings and investment in the nation, as higher savings and investment result in higher economic growth (Hunt, 2007). The framework provided by dual-gap analysis demonstrates how investment is necessary for national development but that there are inadequate domestic savings to support such expenditures (Hassan, Sule & Abu, 2015).

Most empirical investigations on deficit financing have raised conflicting arguments, conclusions and even further research. Alam, Sadedin, Islam, and Moudud-Ul-Huq (2022) explored the level of influence budget deficit financing has on the Bangladeshi economy from 1981-2018. The study employed the cointegration test, vector error correction mechanism (VEM), and Granger causality test. The results show that the variables are co-integrated and, so, have a long-run nexus. Domestic debt, money supply and external debt all have positive long-run effect on economic growth. Chinemerem, EO and Bruno (2022) investigated the impact of deficit financing on Nigerian sectoral output from 1986 to 2020. Using the ARDL technique, the study found that domestic debt has a significant positive effect on sectorial output but foreign debt has a tiny impact on manufacturing sector output. Ajiboye (2022) investigated the impact of Nigeria’s fiscal deficit on economic growth. From the findings, there exist significant and positive connection between deficit financing and economic growth in Nigeria. Olusegun et al., (2020) investigated the influence of external debt on Nigerian economic growth between 1981 and 2018. ARDL and ECM estimation methodologies are used and the result revealed that external debt stock, domestic debt stock, foreign direct investment, and government expenditure are all important aspects of Nigeria's economic growth. Ifeanyi and Umeh (2019) investigated the influence of deficit financing on economic growth in Nigeria from 1981 to 2016. The result proved that external debt is a kind of deficit financing that impedes Nigerian economic growth; however, domestic debt stimulates economic growth, with debt service having no effect on Nigerian economic growth. Okah et al., (2019) examined the influence of deficit financing on economic growth rate in Nigeria from 1987 to 2017. The analysis signify that deficit funding will only marginally aid Nigerian economic advancement. Omoderogu et al., (2020) analyzed the impact of Nigeria's external debt on economic growth from 1995-2017. Using the OLS technique, the outcome established that a positive but insignificant link exist between foreign debt stock and the GDP, a negative and insignificant link exist between foreign debt servicing and the GDP, and a positive

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and substantial relationship exist between Inflation Rate and the GDP. Odubuasi et al., (2018) used Granger Causality and Johansen Co-integration estimation technique to examine the influence of external debt on Nigerian economic growth from 1981 to 2017. The result showed that external debt stock and government capital investment have a favorable impact on Nigeria’s economic growth, however external debt servicing has no meaningful impact. Shkolnyk and Koilo (2018) used the ARDL model and correlation analysis to analyze the relationship between foreign debt and economic development in emerging economies between 2006 and 2016; and found that external debt had no effect on the economic growth of the countries studied. Ali, Mandara, and Ibrahim (2018) examined the influence of deficit financing on economic growth in Nigeria from 1981 to 2016. From the analysis, deficit financing stimulates output growth. Fagbohun (2017) examined the impact of budget gaps on economic growth in Nigeria from 1970 to 2013. Using the least square-OLS method, the results revealed that budget deficits and external reserves both contribute to rising per capita income, whereas bank rates and money supply do not. Ugwu (2017) examined the relationship between domestic debt and economic growth in Nigeria between 2000 and 2016. The findings show that outstanding domestic debt has a strong and positive association with GDP (economic growth) in Nigeria, and they advocate keeping the domestic debt-bank deposit ratio under 40% and providing an enabling environment with enhanced infrastructure.

3. METHODOLOGY

The investigative econometric research design, also known as the "Ex-post Facto Hypothetico-Deductive Methodology," was utilized. It is a non-experimental design that compares pre-existing groups on a dependent variable. The 53 Sub-Saharan African nations made up the research’s population (World Bank, 2021), as do all economic factors related to government’s use of deficit financing. However, the purposive sampling technique was adopted which comprises of the four largest economies in Sub-Saharan African countries namely: Nigeria, Kenya, South Africa, and Cameroon (Didia & Ayokunle, 2020). Secondary panel series from 1986 to 2021 was obtained from World Bank Report and the statistical database of the Central Bank of Nigeria (CBN). Descriptive statistics, Hausman and Panel Ordinary Least Square techniques were utilized to analyze the data; at the 5% level.

The model was based on the combination of the Keynesian General Theory (2016) of Deficit financing and debt theory; and fiscal responsibility theory and is stated as follows: The first equation is that the Real gross domestic product is a function of budget deficit; this is because the selected African countries mainly operate on a budget deficit which transcend to use of deficit financing mechanism as sources of funding for their budgets. Thus, this study seek to examine budget deficit in Sub-Sahara African countries and its influence on economic growth rate over the years. In line, the functional form of the model is:

\[ RGDP_t = f(BUD_t) \]  \hspace{1cm} 1

The second equation deals with the various deficit financing mechanisms adopted by these countries in funding their budget. It is stated as;

\[ RGDP_t = f(EXD_t, DOD_t, EXR_t) \] \hspace{1cm} 2

Converted to an econometric form by the introduction of the \((\beta_t)\) and \((\alpha_t)\) and error term \((\sigma)\) and \(\mu\):

\[ RGDP_t = \beta_0 + \alpha_1EXD_t + \alpha_2DOD_t + \alpha_3EXR_t + \mu_t \] \hspace{1cm} 3

The data was logged for uniformity of the variables. The log-linear equation is:

\[ \text{LnRGDP}_t = \beta_0 + \alpha_1\text{LnEXD}_t + \alpha_2\text{LnDOD}_t + \alpha_3\text{LnEXR}_t + \mu_t \] \hspace{1cm} 4

\(RGDP\) = Real gross domestic product, \(EXD\) = External debt, \(DOD\) = Domestic debt, \(EXR\) = External reserves, \(BUD\) = Budget deficit, \(\beta_0\) = Constant Term, \(\alpha_1, \alpha_2, \alpha_3\) = Coefficients of Predictors, it = Cross sectional panel series, Ln = Natural Logarithm, \(\mu\) = Error terms

Apriori expectation: on the average, this study expects that \(\alpha_1, \alpha_2, \) and \(\alpha_3 > 0\); and \(\beta_1 > 0\); signifying a significantly positive linear relationship amongst the variables.

4. RESULTS AND DISCUSSION

4.1 Descriptive Summary

Table 4.1 below shows that the p-values of the Jarque-Bera test for GDP, domestic debt, external debt, external reserves, and budget deficit are greater than the level of significance chosen at 5%, hence, they are normally distributed. Also, the percentage of deviations from the mean values show that the variables had varying periods and were very instable.

<table>
<thead>
<tr>
<th></th>
<th>LNRGDP</th>
<th>LNDOD</th>
<th>LNEXD</th>
<th>LNEXR</th>
<th>LNBUD</th>
</tr>
</thead>
</table>
4.2: Hausman Test for Budget Deficit
The results of the Hausman test for the optimal model choice between Fixed Effects Models and Pooled Ordinary Least Squares (POLS) are shown in Table 4.2 below. The Fixed Effects model was chosen over the Random Effects model because the Hausman test’s p-value of 0.0074 is below the 5% level of significance.

Table 4.2:

<table>
<thead>
<tr>
<th>Test summary</th>
<th>Chi-Sq. statistic</th>
<th>Chi-Sq. d.f.</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cross-section random</td>
<td>7.181421</td>
<td>1</td>
<td>0.0074</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Cross-section random effects test comparisons:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>LnBudget Deficit (LnBUD)</td>
</tr>
</tbody>
</table>

Source: E-view Output

4.3: Hausman Test Result for Deficit Financing
From table 4.3 below, the Fixed Effects model was chosen because the probability value of the Hausman test is less than the 5% significance level.

Table 4.3:

<table>
<thead>
<tr>
<th>Test summary</th>
<th>Chi-Sq. statistic</th>
<th>Chi-Sq. d.f.</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cross-section random</td>
<td>1447.537632</td>
<td>3</td>
<td>0.0000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Cross-section random effects test comparisons:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>LnEXD</td>
</tr>
<tr>
<td>LnDOD</td>
</tr>
<tr>
<td>LnEXR</td>
</tr>
</tbody>
</table>

Source: E-view Output

4.4: Fixed Effect Regression Result for Budget Deficit
The fixed effect regression results demonstrate that the budget deficit (LnBUD) is negative (-0.114603) and significant (0.0204) to gross domestic product. This means that for every unit increase in the Sub-Saharan African countries’ budget deficit, their gross domestic product will fall by 0.114603 unit. Also, budget deficit contributed to the variation in gross domestic product. This finding is supported by the F-value of 309.4378, which is significant at the 5% level as indicated by the F-p-value statistics of 0.000000. The significant F-value also indicates that the model is reliable and can be utilized to develop meaningful conclusions. The adjusted R-squared of 0.909342 indicates that budget deficit account for approximately 90.9% of the variation in Sub-African countries’ gross domestic product, while the remaining 9.1% is due to additional factors not captured in this study. Still, the Durbin-Watson value of about 1.595189 indicates that the model is free of first order autocorrelation.

Table 4.4:

<table>
<thead>
<tr>
<th>Dependent variable: LnRGDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>LnBudget Deficit</td>
</tr>
<tr>
<td>C</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Effects Specification</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cross-section fixed (dummy variables)</td>
</tr>
<tr>
<td>Adjusted R-squared</td>
</tr>
<tr>
<td>Durbin-Watson stat.</td>
</tr>
</tbody>
</table>

Source: E-view Output
4.5: Fixed Effect Regression Result for Deficit Financing

From table 4.5 below, the coefficient of External debt in Nigeria is negative and insignificant to the gross domestic product of sub-Saharan African countries. This means that for every unit increase in Sub-Saharan African external debt, the region's gross domestic product falls by 0.005154 unit. Domestic debt, on the other hand, is positive and significant in relation to GDP. This means that for every unit increase in domestic debt in Sub-Saharan African countries, gross domestic product rises by 0.074780 unit. External reserve is positive and also significant to GDP. This means that for every unit increase in external reserve, the gross domestic product of Sub-Saharan African nations rises by 0.391917 unit. Furthermore, the regression results demonstrated that domestic debt, external debt, and the external reserves all contributed to the variation in gross domestic product. This finding is supported by the F-value of 603.8106, which is significant at the 5% level as indicated by the F-p-value statistics of 0.000000. The significant F-value also indicates that the model is constant and can be applied to derive meaningful inferences. The corrected R-squared of 0.966336 implies that domestic debt, external debt, and external reserves account for approximately 96.6% of the variation in Sub-Saharan countries' gross domestic product, while the remaining 3.4% is due to other dynamics not depicted in this study. Furthermore, the Durbin-Watson value statistic reveal that the model is free of first order serial correlation.

<table>
<thead>
<tr>
<th>Dependent variable: LnRGDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>LnEXD</td>
</tr>
<tr>
<td>LnDOD</td>
</tr>
<tr>
<td>LnEXR</td>
</tr>
<tr>
<td>C</td>
</tr>
</tbody>
</table>

**Effects Specification**

**Cross-section fixed (dummy variables)**

<table>
<thead>
<tr>
<th></th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Probability value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adjusted R-squared</td>
<td>0.966336</td>
<td></td>
<td></td>
<td>603.8106</td>
</tr>
<tr>
<td>Durbin-Watson stat.</td>
<td>1.608463</td>
<td></td>
<td></td>
<td>0.000000</td>
</tr>
</tbody>
</table>

**Source: E-view Output**

4.6 DISCUSSION OF FINDINGS

From estimations done using the appropriate analytical techniques, the findings of this research is discussed as:

First, sub-Saharan African countries' domestic debt greatly boosts economic growth. This suggests that the rising domestic debt in this region has potentials for robust economic growth proving that when governments use borrowed credit for development goals, the aftereffect is increased economic growth. Furthermore, the preceding research established that domestic borrowings do not always hinder economic growth. This is because, at low debt levels, extra foreign borrowings may increase growth to the extent that the additional capital supported by this new borrowing improves the country's productive capacity. As a country's availability to loans decreases, so does its inclination to save, and as a result, the economic process is slowed. However, this study does not recommend for soliciting overseas loans in order to service past loans obtained. This supports the findings of Solawon & Adekunle (2018) and Sulaimand & Azeez (2012). Second, external debt stifles the growth of Sub-Saharan African economies. This suggests that a unit increase in external debt in Sub-Saharan African nations might reduce economic growth by 0.005154 unit. The implication of this conclusion is that the majority of Sub-Saharan African countries' foreign borrowing has not been put to productive use in their country. Furthermore, it appears that in order to service their debt and repay principle sums, Sub-Saharan African countries have crowd-out private investment by obtaining domestic loans from financial institutions. This supports the findings of Nwanna and Umeh (2019), Ifeanyi and Umeh (2019), and others who have found that external debt is negatively and strongly associated to economic growth. However, it contradicts the findings of Solawon and Adekunle (2018) and Sulaiman and Azeez (2012), who found that foreign debt is positively and strongly associated to economic development. Third, sub-Saharan African countries' external reserves greatly boost economic growth. This means that every unit increase in external reserves causes the economy of Sub-Saharan African countries to grow by 0.391917 unit. This implies that the federal governments of the various countries should make concerted efforts to create foreign reserves in order to complement government expenditure; as a result, their economies will improve greatly. This is consistent with the findings by Tung (2018) that external reserves harmonizes fiscal deficits and makes an economy’s growth to be consistent. Finally, budget deficit is negative and significant in terms of Sub-Saharan African economic growth. This suggests that a 1% increase in budget deficit financing will cause the economies of Sub-Saharan African countries to contract significantly by 0.03420%. This shows that the Sub-Saharan countries’ fiscal practices have hampered their economic growth. This is because the resources accumulated through the budget deficit and its funding mechanism in Sub-Saharan Africa have not been put to good use (Iya, Aminu & Gadbo, 2014; Nwanne, 2014).

5. CONCLUSIONS AND RECOMMENDATIONS
The aim of this report is to look into the effects of deficit finance on economic growth in Sub-Saharan African countries from 1986 to 2021. Gross domestic product, domestic debt, external debt, external reserves, and the budget deficit are the variables used in this analysis. For a robust analysis, the descriptive statistics, Hausman test, and fixed effect test are utilized in the study. The statistical estimations show that Domestic debt and external reserves are the two most important deficit financing drivers affecting economic growth in Sub-Saharan African countries, according to the study. As a result, there exist an impact on the growth rate of Sub-Saharan African economies.

The study concludes that external debt and budget deficit are detrimental to the economic growth rate because the majority of her foreign borrowings has not been put to productive use in the various countries. Furthermore, in order to service her debt and repay principal sums, Sub-Sahar African countries have crowd-out private investment by obtaining domestic loans from financial institutions. Additionally, the resources accumulated through the budget deficit and its funding mechanism in Sub-Saharan Africa have also not been effectively employed.

Consistent with the results, the following recommendations are proffered:

i. Financial agencies of Sub-Saharan African countries should maintain an optimal level of domestic debt because it is one of the mechanisms for economic growth.
ii. Governments’ monetary and fiscal agencies in the region should ensure that all initiatives to reduce the country's external reserves are opposed.
iii. The budget deficit should be kept at sustainable levels by looking into new ways to finance spending, particularly development spending, such as public-private partnerships, which will create fiscal space off the government's balance sheet.
iv. These agencies should pause using foreign borrowing to finance budget deficit because it does hampers economic growth through crowding-out of private investment funds.

REFERENCES


