

THE EXISTENCE AND NATURE OF
THE CROWDING OUT EFFECT IN KENYA //

by

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ABSTRACT

The rapid growth of the public sector is a feature characteristic of many developing countries. In Kenya, this aspect has continued unabated since Independence; causing concern among policy makers about the implications of such growth, especially of expenditures, for the economy in general, and the private sector in particular.

Economic Theory suggests that in the public-private sector interrelationship, the rapid expansion of public sector spending might be at the expense of the private sector's - a situation referred to as the crowding out effect. This Paper studies this phenomenon for Kenya by way of analysing its major aspects, i.e. the financial, real investment and price crowding out effects (as they affect private sector enterprises expansion).

The results indicate that the phenomenal growth in the domestic deficit financing of public sector spending, has crowded out private sector enterprises' borrowing from the financial market through non-price rationing mechanisms; while the impact of public sector real investment on private sector real investment, though partially expansionary is not statistically significant as a determinant. The price

crowding out effect is not statistically significant either. However, the pattern of public sector investment spending has completely crowded out the private sector in the industry: Electricity and Water; in other industries the crowding out effect is either partial or indeterminate.