

**EFFECT OF FISCAL POLICY VARIABLES ON PRIVATE
INVESTMENT IN KENYA**

CECILIA NJERI CHEGE


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DECLARATION AND RECOMMENDATION

Declaration


This thesis is my original work and has not been presented for award of a diploma or conferment of degree in this or any other institution.

Signature.....
Cecilia Njeri Chege
CM12/29087/17


Date..... 24/10/2024

Recommendation

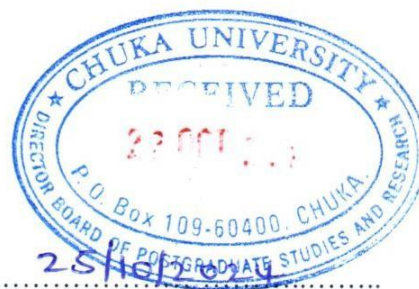
This thesis has been examined, passed and submitted with our approval as the University Supervisors.

Signature.....
Dr. Lenity Maugu, PhD
Chuka University

Date..... 25/10/24

Signature.....
Dr. Onesmus Mbaabu, PhD
South Eastern Kenya University

Date..... 25/10/2024



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DEDICATION

I dedicate this thesis to my dear Husband Armstrong, my lovely sons Jayden and Liam and to my caring and loving mother Hannah.

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ABSTRACT

The tenacity of the country's entrepreneurs and the favorable climate has been credited with the rapid expansion of private sector activity in the Kenyan economy. New technology and increased private investment propel the country's economy toward full employment, where resources are best used and economic development is achieved. Investment levels should be over 32 percent of Gross domestic product, with state investment comprising above 9 percent of Gross domestic product and private investment being 24 percent of Gross domestic product, according to Vision 2030. This objective does not appear to be attainable at the current growth pace. Several studies have examined the nexus between fiscal policy variables and private investment. However, there are mixed findings across countries and regions. For instance, some studies find a positive relationship, others find an insignificant effect, while others find a negative relationship. The contrasting findings could be due to differences in methodology, measurement of variables or country specific differences. Kenya has a dynamic economy with unique characteristics. It is therefore necessary to conduct further study in the country using a robust methodology and recent data. This study contributes to the existing literature by providing an empirical investigation of the effect of fiscal policy variables on private investment in Kenya using data covering the period of 1980- 2022. The specific objectives were; development government expenditure, recurrent government expenditure and corporate tax effect on private investment in Kenya. The study's theoretical foundations included the Keynesian Approach (Crowding in and crowding out) model and the Neo-classical Approach Theory (Tobin's Q 1969). To find the casual effect link between the variables, a casual study design was used. A sample of 42 years from the yearly series data was taken from the websites of the African Development Indicators, Kenya National Bureau of Statistics, and Kenya Revenue Authority for the years 1980 to 2022. The study employed the autoregressive distributed lag (ARDL) model and the ECM was estimated since there was cointegration. It was found that development government expenditure had a positive (1.3860) significant effect on private investment in the short run and a negative (-1.2120) insignificant effect on private investment in the Long run. This could have been attributed to by factors such as efficient resource allocation in the short run. Government spending on infrastructure, Social security, education, research and technology has a positive effect on private investment. There was a negative (-0.3631 and -2.7596) significant effect of recurrent government expenditure both in the short run and Long run respectively on private investment in Kenya. This implies that more government spending on recurring costs may increase the demand for borrowing by the government, which would raise interest rates hence, crowd-out private investments. The findings demonstrated that corporate tax had a significant negative (-0.3088) effect on the short run and positive (0.4161) effect on the Long run on private investment in Kenya. A rise in corporate taxes immediately raises a company's short-term investment costs. Higher taxes lower businesses' after-tax profits, which may deter them from expanding their operations or making new investments. In the long run, businesses might eventually modify their tactics to account for increased taxes. This entails streamlining their operations to lessen the effect of taxes on investment, maximizing their capital structure, or looking for tax breaks. According to the study, the government is recommended to allocate funding for development in a balanced manner that considers both the short-term and long-term benefits of stimulation. It suggests that the government implement changes to lower costs and improve the efficacy of ongoing expenditures. This means reducing bureaucracy, optimizing staffing levels, and streamlining the procurement process. In order to facilitate

investment planning, a consistent corporation tax policy may be implemented by allocating revenue money to worthwhile endeavors that will increase private investment in Kenya. Future studies may be done targeting other variables as well as in other countries.