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The Relationship between Defense Expenditures and Economic Growth in Sri Lanka: A Causal Analysis

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Abstract

The purpose of this research is to investigate the causal relationship between economic growth and defense expenditure in Sri Lanka over the period 1950- 2006. This study employs Granger –Causality tests using annual time series data to analyze the presence and direction of causality between economic growth and defense expenditure. In addition to analyzing causality, the study focuses upon the appropriate representation of the nature of nonstationaries apparent in these two economic timeseries. Moreover, cointegration testing and error correction mechanism also used to analyse the long run relationship between the two variables. The result suggests that there is a unidirectional causal relationship between economic growth and defense expenditure. That is economic growth causes military expenditure in Sri Lanka.

1 Introduction

Defense expenditure in developing countries has increased rapidly in the last two decades. This trend can cause low economic performance, increasing poverty and deprivation, less development, etc. That military expenditure³ has an impact on economic growth has made most of the researchers to analyze the relationship among them. This relationship

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3 Military/ defense expenditure is used here to refer the direct cost of war. Throughout this research, we will use military expenditure and defense expenditure interchangeably