# MACROECONOMIC VARIABLES AND ECONOMIC GROWTH IN SRI LANKA: A TIME SERIES ANALYSIS

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The main objective of the study is to investigate the empirical relationship between macroeconomic variables and economic growth in Sri Lanka. Exchange rate, inflation, government spending, and unemployment rate were considered as macroeconomic variables. Changes in gross domestic product were considered as an indicator of economic growth. The current study used annual time series data over the period from 1990 to 2019 which were collected from the annual reports of the Central Bank of Sri Lanka. Stationary of the data was tested using the Augmented Dickey-Fuller test. Johansen co-integration test, Vector Error Correction Model, and Granger causality test were used to estimate the relationship between macroeconomic variables and economic growth. The results of the Vector Error Correction Model revealed that inflation has a significant long-run impact on economic growth, while exchange rate, government spending, and unemployment rate have not significantly influenced economic growth in the long run. However, the Granger causality test revealed that the exchange rate, inflation, and unemployment rate have a significant impact on economic growth in the short run. The results support the theoretical prediction that macroeconomic variables would play an active role in economic growth. The study, therefore, concludes that macroeconomic variables are driving economic growth in Sri Lanka. Therefore, growth-oriented macroeconomic policies should be established for protecting poor people in the country.

**Keywords:** *Macroeconomic variables; Economic growth; Vector error correction model; Sri Lanka*