IJEFI

INTERNATIONAL JOURNAL OF ECONOMICS AND FINANCIAL ISSUES

EJ EconJournals

ISSN: 2146-4138

International Journal of Economics and Financial Issues

ISSN: 2146-4138

available at http: www.econjournals.com

International Journal of Economics and Financial Issues, 2016, 6(4), 1973-1980.

EJ EconJournals

Determinants of External Debt in Thailand and the Philippines

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ABSTRACT

External debt (ED) has been the major global concern not only heavily indebted poor countries but also developing nations in resultants of the 2008 global financial crisis. It has become a well-discussed subject and generally a concern of global finance and world of economy greatly. This paper analyses the role of some macroeconomic variables in determining the ED burden in Thailand and the Philippines from 1976 to 2013. The results indicate the existence of short-run linkages originated from inflation rate (Consumer Price Index [CPI]) and real interest rate [RIR] to ED in the case of Thailand. As for the Philippines, although there is no evidence of short-run linkages origin from gross domestic product (GDP), CPI, RIR and M2 to ED, but the burden of short-run adjustment appears to have fallen mostly on GDP and M2. Further, dynamic econometric analysis suggests that money and quasi money (M2) to total reserves ratio is the most exogenous variable beyond the 50-years horizon. The study concludes that a sound debt management could be implemented to control debt accumulation and to reduce dependence on debt relief in the form of foreign aid.

Keywords: External Debt Burden, Thailand, The Philippines
JEL Classifications: F34, C22

1. INTRODUCTION

Foreign indebtedness has continuously become a debatable issue for policy makers and researchers and in the broader international community since the outbreak of the sovereign debt crisis in the European countries in 2009. While external factors seem to be the most profound aspects that affect the external indebtedness of poor nations, there is still a continuing debate on the determinants of the foreign borrowing by developing countries. In this aspect, the problem of external debt (ED) in most of the developing countries is believed to be one of the major challenges nowadays. Although it is believed that ED can assist nations that are suffering from capital deficiency to achieve accelerated economic growth, however, once this financial gap becomes unmanageable, the past-accumulated ED is likely to provoke further external borrowings and this will create another vicious circle of ED (Tiruneh, 2004; Awan et al., 2015).

Throughout the years, debt has been an old issue for the Philippines but it is constant problem as indebtedness and debt service payments continue to grow. The ED has rose gradually over the 1976-1986 in the Philippines and reached about 94% of gross domestic product (GDP) in 1986 (Figure 1). It is mainly because of deep economic and political crisis that started in the late 1970s. This crisis has brought serious macroeconomic manifestations including high inflation, large current account deficits and huge arrears in ED (World Bank, 1996). Therefore, the Philippines indebtedness is the consequence of past policy mistakes, debt mismanagement, and historical conditions that involved heavy borrowing (Boyce, 1992; Vos and Yap, 1996).

On the other hand, Thailand foreign indebtedness was not exceedingly high in 1970s to 1980s relative to the Philippines. Nevertheless, it increased significantly in the early 1990s as a reflection of persistently high current account imbalances. The ED has rose from less than 40% during 1990-1992 to more than 60% during the period of 1996-1997 and peaked at 94% of GDP in 1998. Thailand relied on foreign capital to finance the gap between domestic savings and investment, but high current account deficits and the subsequent high external indebtedness were excessive compared to the growth path of the Thai's economy and this eventually led to the Asian Financial Crisis in