

Chapter 75

The Impact of Globalization on External Debts: Evidence From Developing Countries

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ABSTRACT

In this chapter, the answer to this question has been researched theoretically and empirically. KOF Globalization Index has been used as the measure of globalization unlike the empirical literature that explores the relationship between globalization and external debt. In the study where panel data analysis method has been used, the findings show that there is a positive relationship between KOF Globalization Index and external debt in developing countries. When it is examined from the perspective of the sub-indexes of globalization, it is seen that the economic globalization index is positively related to external debt. Social and political globalization has no effect on external debts. Impact of the control variables used in the analysis on external debts is significant and negative. From this, it can be said that general globalization and economic globalization have increased the external debt of the nations.

INTRODUCTION

One of the main macroeconomic problems of underdeveloped and developed countries in the world is increasing external debt. In these countries, the failure of supplying the investments required for the acceleration of economic growth from domestic sources (insufficient domestic savings and foreign exchange shortfall) have increased the need for external debt. This need has emerged after World War II and the Developing countries turned to external sources and external borrowing especially after 1970. External borrowing, which is regarded in classical theory as a form of financing to be resorted to under extraordinary circumstances, has evolved into a standard practice because of the changing economic conditions of the day. Liberalization of capital movements starting from the second half of the 1980s as well as the acceleration of globalization starting from the middle of the 1990s increased the dependence

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of the countries on each other and the need for loans; and, in this regard, credit facilities were expanded while low cost and affordable borrowing options were created as well. In the past thirty years, there has been an increase in public debt stock in most developed countries. For example, public debt stock in OECD countries were about 30% of GDP in the early 1980s but then rose to 50% in 2005. Is globalization really an important factor in increasing external debt of the nations - limiting their economic growth- as suggested by some authors and mentioned here as well?

Globalization, one of the key concepts of the twenty-first century, is one of the most debated concepts. While the analyses of world capitalism proceeded on an international basis until the 1980s, this internationally based process was substituted by the globalization as a result of an intense paradigm change (Heywood, 2014, p. 27). Globalization can be expressed as a process in which common values in economic, political, social and cultural spheres spread across the world beyond the national borders. So; globalization is a multidimensional concept and the definitions vary depending on from which discipline it is handled.

Globalization is different from such similar concepts as internationalization, liberalization, universalization or westernization. However; these concepts are close to each other and sometimes used interchangeably (Gygli, 2018). Globalization is a phenomenon that includes liberalization, internationalization and universalization but also exists everywhere with its economic, social, political, cultural and ideological impacts. As McGrew (2010) also put it simply, globalization means the expansion, deepening and acceleration of mutual links around the world. According to Dreher (2006), who introduced KOF globalization index, “it is a process of creating networks of connections among intra- and multi-continental distances, mediated through a variety of flows including people, information and ideas, capital, and goods. Globalization is a process that erodes national boundaries, integrates national economies, cultures, technologies and governance, and produces complex relations of mutual interdependence.” According to another definition, globalization refers to the spreading of some common values in economic, political, social and cultural spheres beyond the local and national borders across the world (DPT, 2000, p.3). This new process led to liberal economic order in the economic arena and liberal political order in the political arena. According to the definition of the World Bank (2000), globalization is “the freedom and ability of individuals and businesses to initiate voluntary economic transactions with the individuals and institutions of other countries.” According to Stiglitz (2015), globalization means the reduction of transportation and communication costs and the integration of national economies by removing the obstacles against the flow of goods, services, capital, labor and information. The most researched dimension of globalization, as defined by the World Bank, is *economic globalization*.

As suggested by Stiglitz (2004), globalization is a process that must be well managed and its impacts are not the same in all countries regardless of which dimension is mentioned, particularly the economic-political sphere. While some countries benefit from globalization at the maximum level by minimizing the risks and uncertainties, some other countries that cannot manage the process well suffer from globalization. In this context; globalization is particularly effective in strengthening the positive impact on economic variables, particularly economic growth, for developed countries with a strong institutional structure, a well developed financial sector and robust macroeconomic policies. Therefore, it is important to know from which perspective the globalization is addressed.

However, regardless of which dimension is mentioned, it can be said that globalization leads to significant changes in many parameters (social, cultural, political, etc.), especially economic parameters (growth, employment, foreign trade, indebtedness, unemployment, inequality, poverty etc.) of the nation states. One of these economic parameters is external debt. In recent years, an increasing number

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