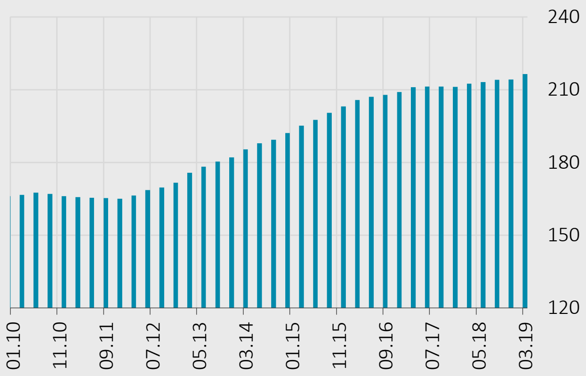
# Box 2.1

## Observations on the Debt Structure of Emerging Economies

The Institute of International Finance (IIF) has released the 2019 first quarter data on global debt stock. This box provides a brief overview of the debt stock data. In the first quarter of 2019, the ratio of the total debt stock to GDP in the emerging market economies (EMEs) that IIF covers[1] remained high, while the rate of increase in the debt, which had decelerated significantly in the preceding year, rose slightly. (Chart 1).

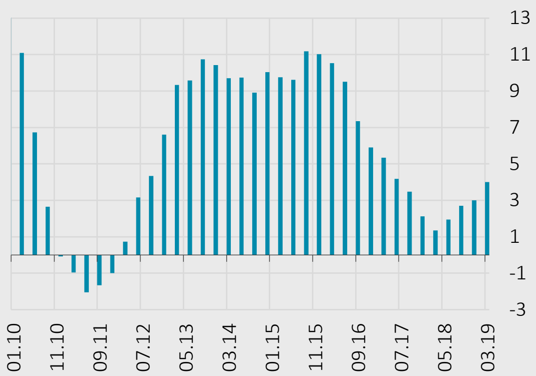
Chart 1: EME 30, Total Debt Stock to GDP

(%)




Source: IIF.

(annual % percentage point change)

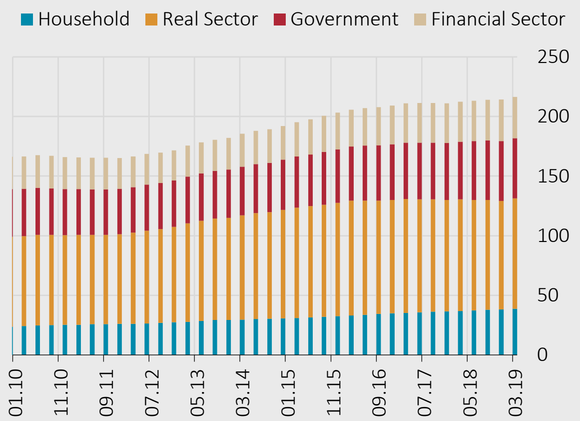



Source: IIF.

An analysis by subsectors indicates that the real sector has the largest share in debt ratio. Since 2017, while the increase in household and financial sector debt to GDP ratio slowed down across the emerging market economies (EMEs), the ratio of real sector debt to GDP declined; the ratio of public sector debt to GDP remained flat (Chart 2).

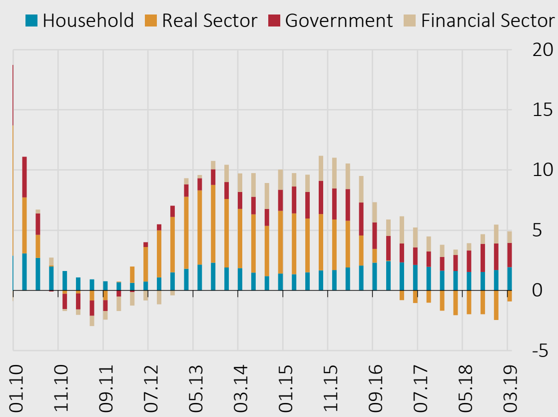
Chart 2: EME 30, Sectoral Debt Stock to GDP

(%)




Source: IIF.

(annual % percentage point change)

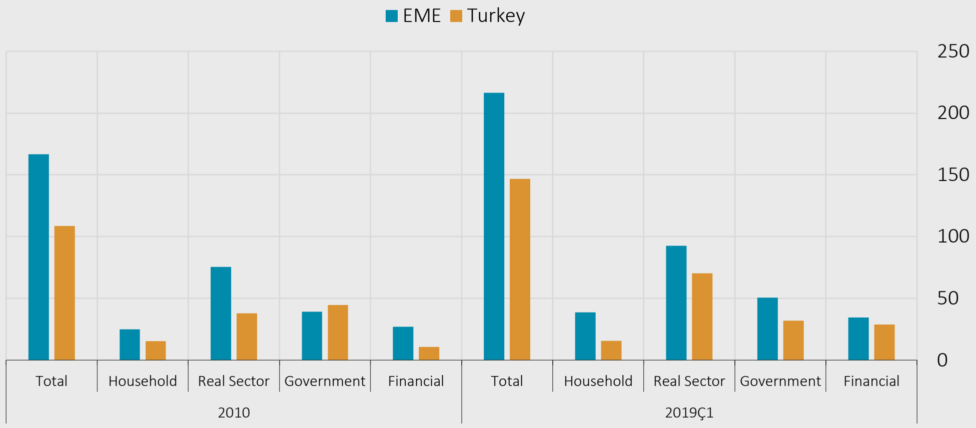



Source: IIF.

[1] 30 EMEs: Argentina, Brazil, Chile, China, Colombia, Czechia, Egypt, Ghana, Hong Kong, Hungary, India, Indonesia, Israel, Kenya, Korea, Lebanon, Malaysia, Mexico, Nigeria, Pakistan, Philippines, Poland, Russia, Saudi Arabia, Singapore, South Africa, Thailand, Turkey, Ukraine, and the United Arab Emirates.

Turkey's total debt stock to GDP was below the EME average both in the first quarter of 2019 and in 2010. Turkey's debt to GDP ratio in all sectors but the public sector remained below the EME average in 2010. However, in the first quarter of 2019, Turkey ranked below the EME averages across all sectors (Chart 3). A sector-based analysis of Turkey's debt stock to GDP reveals significant changes between these two periods. Accordingly, while the public sector debt decreased noticeably, the real sector debt increased. In the same period, while household debt remained low, financial sector debt increased moderately.

Chart 3: Sectoral Debt Stock to GDP, EME-30 vs. Turkey (2010–2019 Q1)

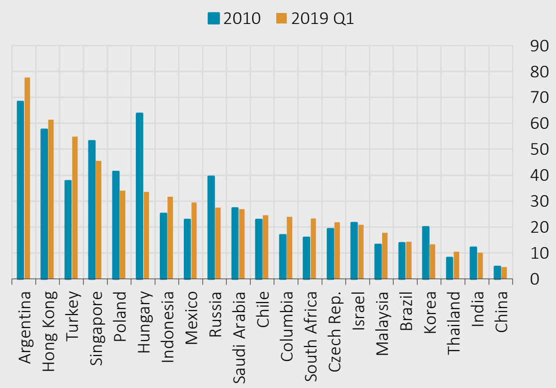



Source: IIF.

Currency decomposition of the total debt stock in EMEs is important in terms of providing guidance on the vulnerability of countries to interest rate and exchange rate shocks. In this context, an analysis of the EME total debt stock in terms of foreign currency-domestic currency breakdown suggests that the share of foreign currency in total debt decreased significantly in Hungary in the 2010-2018 period (Chart 4). With the onset of the 2008 global financial crisis, the Hungarian economy underwent major problems due to non-repayment of foreign currency denominated mortgages. Therefore, a series of measures were put in place in order to deter foreign currency borrowing, which resulted in a considerable decline.

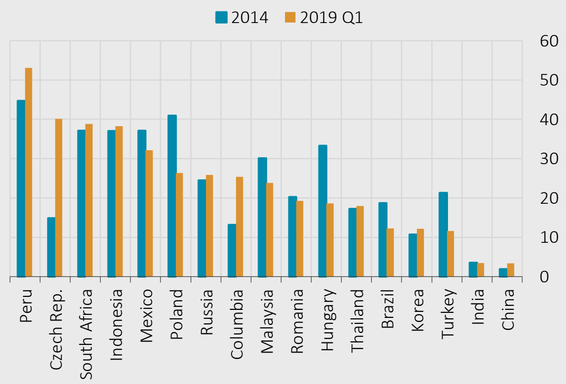
The foreign participation in local currency government bond markets seems to be on the decline in Turkey, Brazil, Mexico, and Malaysia, with Hungary and Poland in the lead (Chart 5).

Chart 4: Share of Foreign Currency in Total Debt Stock, 2010 vs. 2018 (%)




Source: IIF.

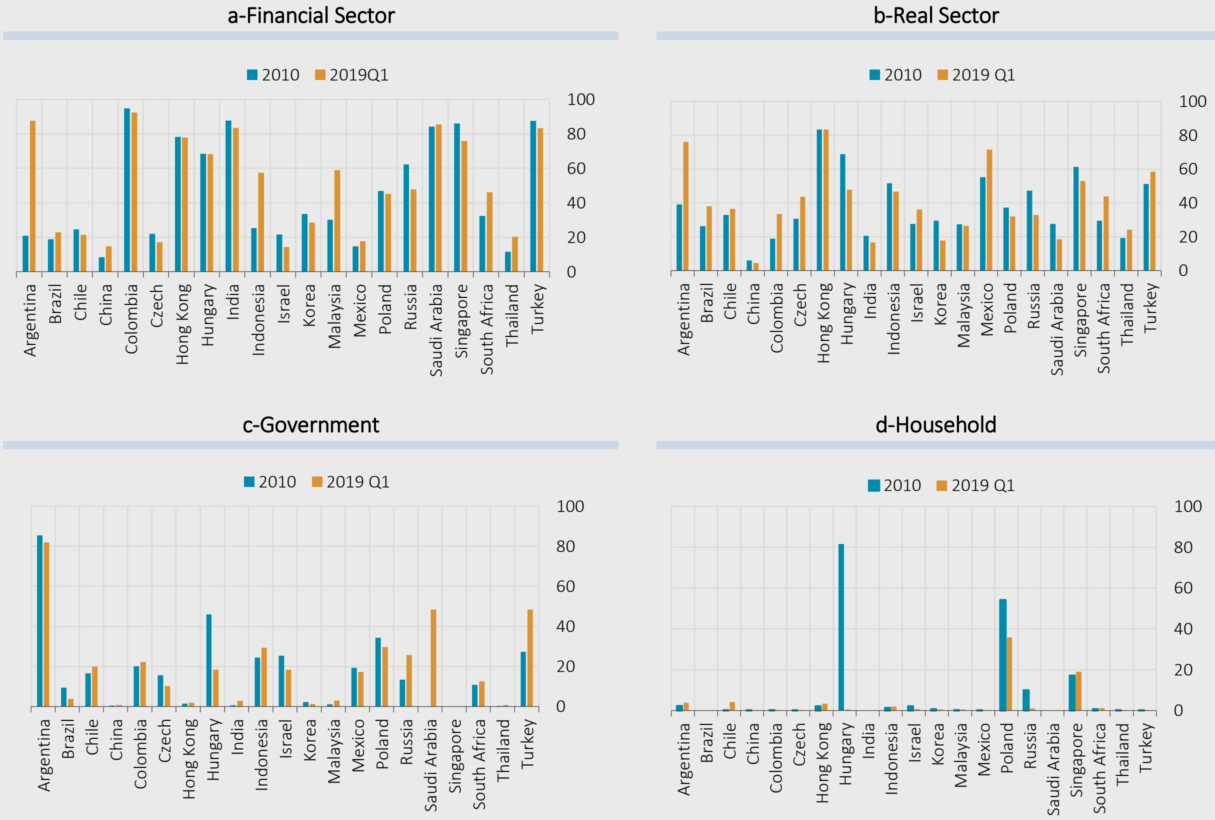
Chart 5: Foreign Participation in Local Currency Government Bond Markets, 2014 vs. 2018 (%)




Source: IIF.

The financial sector has the largest share of foreign currency in total debt across EMEs (Chart 6-a). Especially in Eastern Europe and Asia countries, the financial sector holds more than half of its debt stock in foreign currency. This ratio exceeds 80% in Colombia, India, Singapore and Turkey. On the other hand, the share of foreign currency in the real sector debt stock across EMEs is at more reasonable levels than that of the financial sector (Chart 6-b). However, the share of foreign currency in the real sector debt posted an increase not only in Argentina and Mexico but also in Turkey. The share of public sector debt in foreign currency remains at reasonable levels in countries except for Argentina (Chart 6-c).

Chart 6: Share of Foreign Currency in Total Debt Stock, Sectoral Breakdown




Source: IIF.

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Household foreign currency debt stock is negligible in EMEs due to legal restrictions in place in most of those countries (Chart 6-d). Similarly, it should be noted that foreign currency borrowing of households is subject to legal restrictions also in Turkey. In Hungary after 2010, household foreign currency debt decreased to negligible levels following introduction of legal constraints. In Poland, although the household foreign currency indebtedness, mainly composed of housing loans, has decreased compared to 2010, it remains high. In Singapore, household foreign currency borrowing stems from loans used for housing and partially for durable consumption. However, it should be noted that the foreign currency debt ratio in Singapore is quite low compared to Poland.

In sum, in the first quarter of 2019 across EMEs, while the ratio of total debt stock to GDP remained high, the rate of increase in the debt, which had slowed down significantly during the preceding year, increased slightly. The real sector stands out as the most indebted sector. While the largest share of foreign currency debt in the total debt stock belongs to the financial sector, households have the smallest share in this sense. The share of public sector foreign currency debt stock remains at reasonable levels in countries other than Argentina.