

## INTRODUCTION

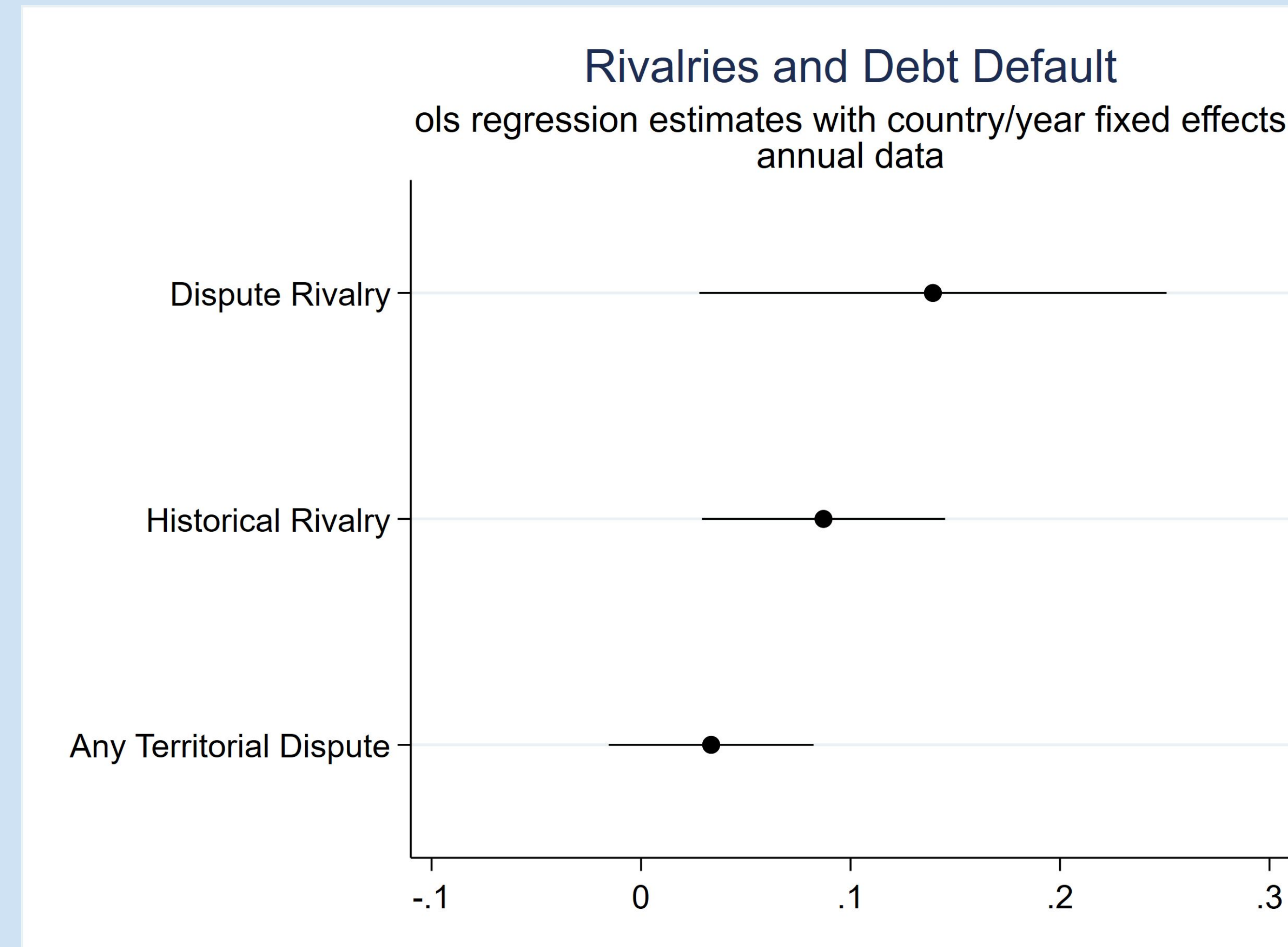
Borrowing is a critical public policy instrument that in the ideal situation allows countries to make investments that increase economic growth and improve the welfare of their citizens. All countries hold some degree of sovereign debt and most have a significant amount of debt. How nations manage their debt is shaped by who they owe money to, whether they budget a surplus or a deficit, and whether they reschedule or default on their debt. Among these decisions, the one with the biggest consequences is default. Understanding what makes countries default can help shed light on what allows countries to borrow in the first place as well as predict future defaults. The political situation inside of a country, the nature of its economic situation and foreign pressures all can shape the decision to default (Tomz & Wright 2007). Security threats are an especially intriguing influence on whether a country defaults on its debt or not due to the variety of effects they could have. Wars demand funding and governments generally have four choices to fund wars: printing money, taxation, internal borrowing and external debts (Pham 2017). While defaulting on their debt may give a country an immediate windfall of money, its long term ability to fund future conflicts would be harmed. I examine this phenomenon by studying long term, enduring rivalries for which it is most likely that the costs of future conflict and need to be prepared influence default decisions (Derouen & Bercovitch 2008).

## RESEARCH METHODOLOGIES

My inquiry approach will be correlational research. Five datasets—one mapping sovereign debt defaults for the past 200 years, one that records all instances of any form of military disputes for the same time frame, one that records territorial disputes between countries, one that records exports and imports between countries and one that measures enduring rivalries based on diplomatic relations—will be used as the data for this project (Reinhart & Rogoff 2011; Palmer et al 2019; Frederick et al 2017; Barbieri et al 2016; Thompson 2001). The Reinhart and Rogoff dataset contains which country years for a large sample of countries from 1820 to 2004 in which there was a default or rescheduling. Whether or not countries default is the dependent variable in the analysis for this project. The second data set—known as the Correlates of War—contains data related to war for all countries since 1815. Most important to this project is the military interstate dispute (MID) data. Using this data set, countries with six or more MIDs with another country in the past 20 years will indicate that the countries have an enduring rivalry during that year. The third data set is similar to the correlates of war data set but only records disputes over territory and includes non-militarized disputes over territory as well. Additionally, the fourth data set records imports and exports for countries which gives additional economic controls. The final data set measures these enduring rivalries by looking at the historical record of diplomacy and attitudes. The dataset created by Thompson bases the start date and end dates of rivalries on explicit threats, enemy perceptions by decision-makers and spatial/territorial concerns.

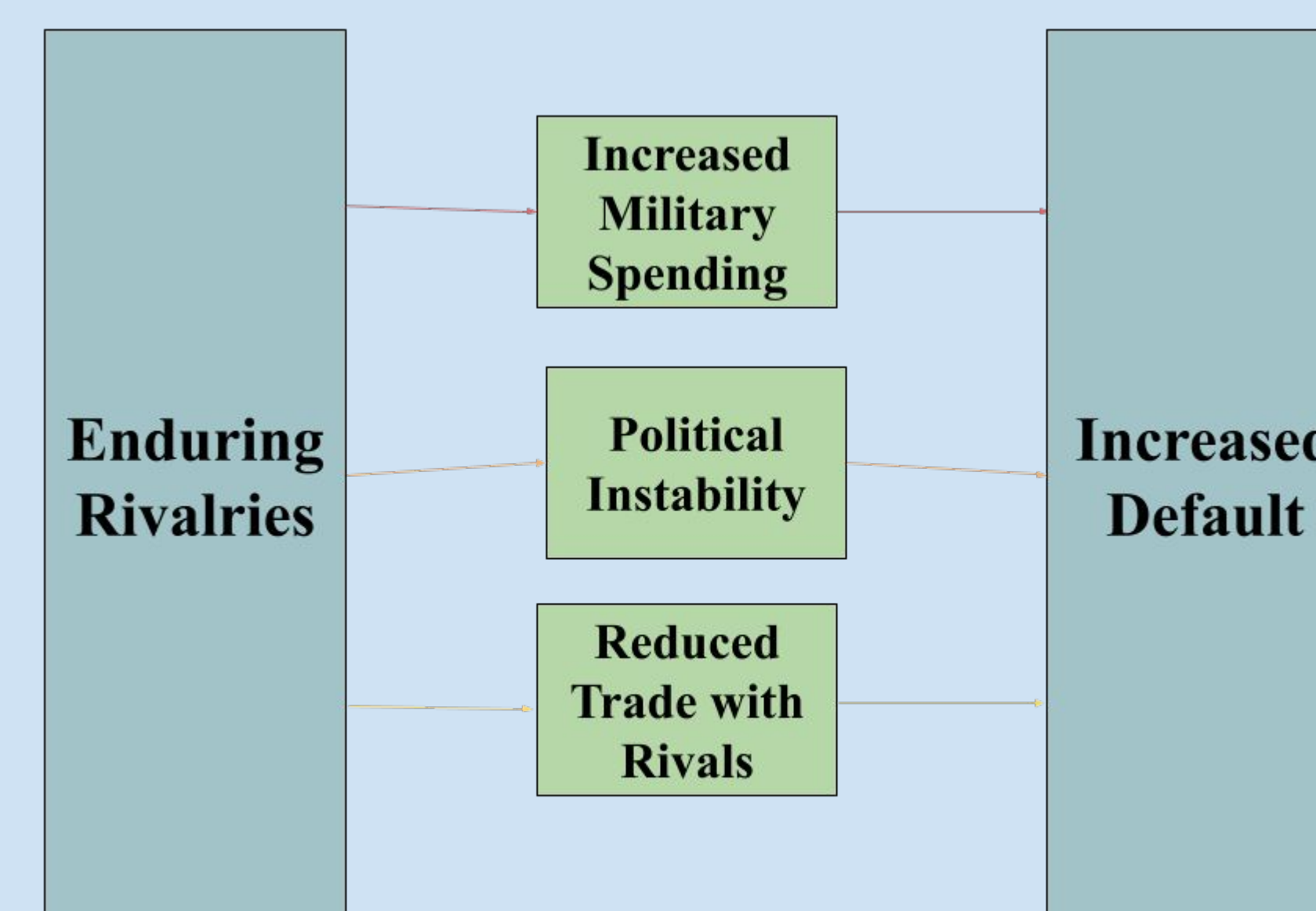
## DATA AND FINDINGS

To evaluate the question of how long term security concerns affects default, the method of analysis is fixed effects linear regression with sovereign default as the dependent variable and one of the three measures of enduring rivalry the key independent variable. In these regressions, I controlled for currency crises, inflation crises, and banking crises and employed year fixed effects to control for common shocks to all countries in a given year and country fixed effects to control for all time constant differences between countries.



For all three measures of enduring rivalry, the estimates indicate a positive correlation suggesting that defaults are more likely when a country has any sort of enduring rivalry. The estimates for the Dispute Rivalry and Historical Rivalry measures are statistically and substantively significant. However, the Any Territorial Dispute measure is not a statistically significant result but does not contradict the other results because the relationship shown is still positive. These results are inconsistent with the idea that countries are less likely to default when they face future conflict and the need to continue to borrow money for those conflicts. The findings are instead consistent with the view that enduring rivalries are harmful to a country and, on average, increase the probability of default.

## CONCLUSIONS AND ANALYSIS



While the relationship between enduring rivalries and default is clearly positive, what cannot be shown by this research design is what mechanism causes this relationship. There are three working theories for how enduring rivalries have this affect. First, that enduring rivalries lead to increased military spending. Second, that enduring rivalries cause increased political instability. And finally these rivalries may reduce trade between nations. All of these factors could help contribute to default. It is possible that all three mechanisms operate to a varying degree or one of them is the most significant reason.

## IMPLICATIONS AND NEXT STEPS

The implications of this project are that countries with long term rivalries are more likely to default on their debt. Of course, lenders should still analyze this on a case by case basis as a country like the U.S. has long standing rivalries yet can still be trusted to pay back their debts.

The next steps for this project were it to continue would be to try to study which mechanism(s) is operating. This could be done by measuring each of the mechanisms and controlling or not controlling for them until the main mechanism is isolated.

## ACKNOWLEDGEMENTS / REFERENCES

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