

How Riba Affect Economic Performance in Cambodia

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Abstract

This study investigates about interest rate to economy including economic growth, investment, and consumption in Cambodia. This study uses vector analysis method with a time period starting from 2000 to 2020 using secondary data from the World Bank. This study investigates the causal relationship between variables including interest rates, consumption, investment and GDP. We found that Interest rates in Cambodia have a negative return on economic growth, this shows that interest rates suppress economic growth and have a significant impact on economic performance in Cambodia. Interest rates also suppress investment and domestic consumption of course this has a bad impact on economic performance. However, an increase in economic growth actually pushed up interest rates. This will result in greater pressure on the economy in the future.

Keyword : Economy, Cambodia, Interest Rate, Economic Growth

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Background

Riba is the so-called excessive and abusive charging of interest on loans. This term is used in finance to denote when a credit or loan demands a high interest rate for borrowing money. Even though it is related to the interest rate on money loans, any disproportionate consideration received in the interest of someone who has entrusted money can be considered usury (Khan, Al Aboud, & Faisal, 2018). Therefore, not only according to liquid money. This term is associated with moral values, not financial or economic ones. Because as long as the lender and the borrower agree, the former can ask for the flowers he deems convenient. However, we must approach it as an abuse of the dominant position of the lender of money. Throughout history, various cultures and religions have strongly rejected usury, some of which, like Islam or Christianity of their time, regarded usury as a crime. With the advent of liberalism, the practice of levies was widespread, but it was considered a crime to prosecute above what would otherwise be logically illegal and socially reprehensible. It's really not very clear what is considered legal and what is not. It depends, to a large extent, on the laws of each country. After all, over the years the law has advanced. Especially in interest of the moratorium. So while it is true that there is no clear boundary in a loan agreement between two parties, there is an interest cap for default. That is, when we are late in our payments and incur additional interest (Prabowo, Sulisnaningrum, & Harnani, 2021).

July 2, 1997, was an unforgettable day for the people of Thailand and Southeast Asia, Because it was the day when the government of Thailand announced the "floating baht" from before, the Thai "baht" will use a fixed exchange rate of 25 baht per US dollar and the announcement of the float baht was the start of the crisis that spread across Asia (Tambunan, 2019). Amid weak

emerging market economies including Thailand where the real estate bubble burst. Meanwhile, the Bank of Thailand (BOT) has been struggling to protect the baht by using international reserves to buy the baht. The “floating” baht policy on July 2, 1997 caused the baht to continue to depreciate (Kulam, 2021). Meanwhile, in August 1997, the Thailand government requested financial assistance from the "IMF" to support the country's economy from bankruptcy (Alfonso Perez, 2021). The depreciation of the baht has become a crisis for the business sector especially large companies that have borrowed foreign money to expand their businesses have more than doubled each company's debt burden and resulted in many companies going bankrupt in Thailand. Of course, in the 1997 - 1998 era, many "employees" of companies and financial institutions "lost their jobs" (Bawono, Zainuri, & Wilantari, 2019).

The Russian-Ukrainian war issues have added fuel leading to a new crisis that many see as Crisis because the covid-19 crisis is not the end. Many businesses are still weak. Revenue has not recovered as it should. had to come face to face with the "energy crisis" that caused the cost of various goods and services to continue, followed by a parade of price adjustments lead to inflation (Božić, Karasalihović Sedlar, Smajla, & Ivančić, 2021). Meanwhile, the Cambodian economy has not recovered strongly. causing many to worry that "stagflation" is high inflation when the economy is growing low. Meanwhile, the world is facing high inflation (Barua, 2021). To fight against inflation, it is estimated that many major economies, especially the United States as the world's number 1 economy, will face an economic recession (Đukić, 2022). While many small countries have high debt ratios. Foreign currency shortages also face bankruptcy as in the case of Sri Lanka (Kariyawasam & Jayasinghe, 2022). However, for Cambodia, lessons from the 1997 crisis caused the Bank of Cambodia to learn and set the card high. Currently, Cambodia's position still has the power to overcome emerging economic problems. Unlike during the 1997 crisis, there was no high foreign debt as in the past. Foreign exchange reserves remain high and financial institutions are strong (Green & Bylander, 2021).

Cambodia's economy may be more vulnerable to inflation and rising interest rates than many other countries. Because debt tends to be concentrated in low-income groups, this is reflected in the problem of high inequality which causes when the debt burden increases according to the interest rate, households need to reduce their consumption (Aiba, Odajima, & Khou, 2018). In addition, Cambodian households have a higher share of the burden of food and energy products than developed countries lead to higher inflation. And in the worst case, high levels of household debt are often a warning sign of a crisis in the financial sector. However, in the short term, it is estimated that there is still a small chance of this happening in Cambodia. Because Cambodia still has strong foreign stability because the current account surplus foreign debt is reduced. Financial institutions are strong and foreign exchange reserves are at high levels (Erokhin & Gao, 2020).

Many cases of economic crises began with the explosion of debt and started from the monetary side. This needs to be examined more deeply to see the impact of interest rates on economic performance, especially on GDP, consumption, and investment (Wilantari, Widarni, & Bawono, 2021). This research looks into the influence of interest rate based on economy including economic growth, investment, and consumption in Cambodia.

Research Method

This study uses vector analysis method with a time period starting from 2000 to 2020 employs secondary World Bank data. This study investigates some causal relationship between variables including interest rates, consumption, investment and GDP with the following model:

$$\begin{aligned}
 IR_t &= \beta_0 + \beta_1GDP_t + \beta_2CO_t + \beta_3I_t + e_t && \text{frm 1} \\
 GDP_t &= \beta_0 + \beta_1IR_t + \beta_2CO_t + \beta_3I_t + e_t && \text{frm 2} \\
 CO_t &= \beta_0 + \beta_1IR_t + \beta_2GDP_t + \beta_3I_t + e_t && \text{frm 3} \\
 I_t &= \beta_0 + \beta_1IR_t + \beta_2GDP_t + \beta_3CO_t + e_t && \text{frm 4}
 \end{aligned}$$

Description :

- IR : Interest rate
- GDP : Gross domestic product
- CO : Consumption
- I : Investment
- E : erroneous title
- t : time sequence
- β : degree in terms of causation influence
- frm: formula

Result and Discussion

We conducted a stationarity test before estimating because the autoregression test required the existence of stationary data. The test results are presented in table 1.

Table 1: ADF's Unit Root Test on IR, EG, CO, and I data in Cambodia

Variable	Unit Root	Include in the examination Equation	Statistics for the ADF Test	5% Critical Value	Description
Interest Rate (IR)	Level	Intercept	-2.823561	0.0489	
	First Diff	Intercept	-5.371131	0.0002	Stationer
Economic Growth (GDP)	Level	Intercept	-0.516717	0.7559	
	First Diff	Intercept	-1.811151	0.2218	
	Second Diff	Intercept	-2.116222	0.0462	Stationer
Consumption (CO)	Level	Intercept	-1.711421	0.2212	
	First Diff	Intercept	-1.722467	0.2539	
	Second Diff	Intercept	-3.261164	0.0262	Stationer
Investment (I)	Level	Intercept	-2.526632	0.1143	
	First Diff	Intercept	-6.432211	0.0000	Stationer

The stationary from the second is GDP with CO, Also IR and I data are stationary on the first difference. We perform optimum lag testing to determine the lag used in vector estimation.

We determine the lag in the estimation based on the optimum lag test results presented in table 2.

Table 2 : AIC result can see from Lag 0 until 4 IR, GDP, CO, with I data in Cambodia

Lag	LogL	LR	FPE	AIC	SC	HQ
0	-122.15565	NA*	3.52126*	12.12313	11.11247	12.12325
1	-89.12123	16.36221	5.15224	11.22332	12.22121	11.11522
2	-59.13322	13.21226	8.72662	11.23251	11.77256	10.76112
3	-29.22521	12.22661	12.22166	13.22351	12.32141	12.32212
4	132.2211	0.000000	NA	-199.2156*	-185.1213*	-192.2212*

After determining the optimal lag, we perform vector estimation which is presented in table 3

Table 3 : The Analysis of the Vector Model

	IR	GDP	CO	I
IR	0.23689 (0.21295) [1.06349]	-0.23132 (0.25232) [-0.74512]	-0.00422 (0.14624) [-0.02417]	-0.03130 (0.02721) [-0.71851]
GDP	0.12617 (1.21341) [0.04451]	-0.37231 (1.33525) [-0.22521]	-0.35421 (1.13759) [-0.15426]	-0.38716 (0.21134) [-1.33126]
CO	-2.52217 (1.51171) [-1.51136]	0.32327 (0.74125) [0.25419]	-0.46115 (0.64421) [-0.72418]	0.008463 (0.12359) [0.04321]
I	-3.23217 (2.11123) [-1.25113]	-0.27151 (1.12211) [-0.21124]	-0.64321 (1.12323) [-0.44123]	0.21125 (0.16231) [0.71125]
C	39.21765 (17.51113) [2.36123]	1.17251 (9.65123) [0.22176]	2.27726 (9.21179) [0.25117]	1.32162 (2.08332) [0.53312]

The connection among IR with IR is greatly positive, the connection among IR with EG is drastically negative, which means when IR are low, then EG will higher. Likewise, the connection among IR with CO are drastically negative, which means that when IR low there is the CO re higher. The connection among IR with I are badly negative, indicating that when low real interest rate will encourage economic growth, and consumption levels are in line with economic growth.

Conclusion

Interest rates in Cambodia have a negative return on economic growth, this shows that interest rates suppress economic growth and have a significant impact on economic performance in Cambodia. Interest rates also suppress investment and domestic consumption of course this has a bad impact on economic performance. However, an increase in economic growth actually pushed up interest rates. This will result in greater pressure on the economy in the future.

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