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Dutch Curse on Indonesia: The Morality of Asian Development Bank (ADB) Loan Projects

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ABSTRACT: Natural Resources Curse, known as Dutch Disease, is because of capital inflow which promotes increase growth and employment level. Indonesia suffers from Dutch Disease working in reverse because of capital outflow, increase unemployment and poverty, and growth retardations from its borrowing from the ADB. I termed this as Dutch Curse because of the colonial connection the Indonesian and Dutch have since the early 17th century. The Dutch Curse is constantly inflicting Indonesia since 1969 because of ADB loans and their disbursement conditionalities. To resolve these issues, it takes more than just the realignment of Indonesia and ADB cooperation, but also moral responsibility and conscious awareness.

KEYWORDS: Dutch disease, Dutch curse, disbursement delays, unsustainable development, negative impact, poverty, unemployment, wealth leakages

JEL Classification: C6, E5, F34, H81, I32, N70

Introduction

> *"If we want to truly understand the convoluted ways in which official aid affects different economic outcomes, we need to plunge into archives, analyse data in detail, carefully look for counterfactuals, understand the temperament of the major players, and take into account historical circumstances. This is a difficult subject that requires detective-like work."* (Edwards 2014).

So, I began my investigation by looking at the historical context of development assistance and the establishment of ADB. Before proceeding, let's see the definition of morality from the Cambridge Academic Content Dictionary (2021) *"a personal or social set of standards for good or bad behavior and character, or the quality of being right and honest."*

Werner (2015, 2) bemused on the outset of development works' strange beginning that coincided when decolonization began in the 1940s. Concurrently, a new study branch of development economics was born. The anthropologist Eric Wolf (1972) argues that capitalism operates in a law that protected ownership of the means of production and to deny access to laborers' products. Thus, the laws function as norms and mechanisms for exerting pressures from more powerful society and the exigencies of the local ecosystem (1972, 2002). This appears to be a powerful analytic approach that lays the foundation for exploring the impacts of capitalism on ecosystems. The ADB operations in all its 68 member countries appear following this pattern through its establishment act that national law must ratify.

In the global capitalism, undeveloped regions were essential to the developed nations' wellbeing because they served as sources of cheap labor, products, and markets for manufactured goods, outlets for cheap capitals for larger profits, and exploitation for poorly paid workers (Edelman & Haugerud 2005, 11). For this purpose, developing countries, including Indonesia, were enticed to be integrated into world capitalism as satellites (or becomes members) for delivering limited, controlled, and unsustainable economic activities for developed countries (Frank 1989). He argues it is part of the plan to keep them undeveloped, subordinated and structurally dependent upon foreign capital and external markets for economic viability (Frank 1989).

Biersack (2006, 9) identified the capitalist initiatives for subordinating the developing countries to a global power structure to make their penetration, which ramifications, are impervious to the layperson's eyes. Wolf (1982) shows that the significance of global capitalist processes affects the local human cultures and environments. He belabored on historical accounts during European colonization, starting around the 1700s and expansion into the Global South in the quest for spicy and minerals that had created the modern economy we are in today. His observation succeeding the Dutch colonization of Indonesia that begun in the early 1600s.

Ecological Debt (or Plunder)

In this article, I draw the exemplum from Wolf's description to expound on the generic phenomenon observed in the ADB's lending operation in which Indonesia as a borrower, has laboured all the conditions to obtain loans to finance its economic development requirements but is denied direct access to the approved loans fund unless it complies with another set of disbursement conditions. I argue that the formation of ADB under the guise of regional cooperation and/or integration is following the subordination pattern described by the scholars referred above by looking specifically at Indonesia's borrowing from ADB and their impacts on Indonesia's economic development indicators. Kathleen J. Hancock (2009) remains us a more detailed description, through her book title *"Regional Integration: Choosing Plutocracy"*. As plutocracy refers to the wealthy entities controlling the government, Hayter (2009 as cited by Baird) plainly expresses *"[t]he actual function of aid from western governments and their agencies, ... is to subsidise the operations of the private corporations and banks of the West."*

Ecologically unequal exchange, or simply means 'plunder' is a concept recently developed as a challenge to mainstream economic theories of trade (Hornborg 1998). Martinez-Alier *et al.* (2014), term this as "ecological debt" to describe the plunder from international trade and their environmental impacts. In this context, I argue that capital flights, both licit and illicit, because of ADB's disbursement delays that normally take more than 7-year, as the product of international trade and agreements, are one form of ecological debt by showing their negative impacts on Indonesia's currency exchange rate, growth, unemployment, and poverty. Pettigrew (1926, 30) shows that banker monopolizes money and credit to plunder the producers of their toils.

Dutch Curse

The Dutch East India Company or *Vereenigde Oostindische Compagnie* (VOC), was state-sponsored merchant operations. They have colonized Indonesia from the early 17th into the 20th century. VOC fostered the spread of—among other—diseases, slavery, bureaucracy, globalization, environmental and cultural destructions, poverty, lack of modern basic infrastructure, and exploitation on an unfathomable scale (Shorto 2013). It gave birth to modern banking, central banks, capital markets, stock exchange, and planted the seed of multilateral co-operations bank to develop colonized lands. During this period, the Dutch generated billions of dollars of capital from Indonesia in various forms—including slave trading—and flown them to the Netherlands. Even today it remains the largest multinational cooperation borne from plundering the wealth, cultures, and environment of its colonies.

Often associated with the natural resource curse, the Dutch disease describes the causative relationship between economic development growth in one sector and a reduction in another. The International Monetary Fund (IMF) described the putative theory as national revenues increase, including those gotten from debt capital, foreign aid inflows induce the strengthening of the national currency gauged from the stability of the exchange rate

(Ebrahim-Zadeh 2003). The theorized impacts would be, among others, increased growth, job creation, revenues, and poverty reduction.

Contrary to the description of Dutch disease, particularly with the capital inflows and strengthening of the national currency, Indonesia's Rupiah suffers from depreciation since 1967 (data from fxtop.com only available from 1967, Figure 1) about the same time it became ADB's members in 1966.

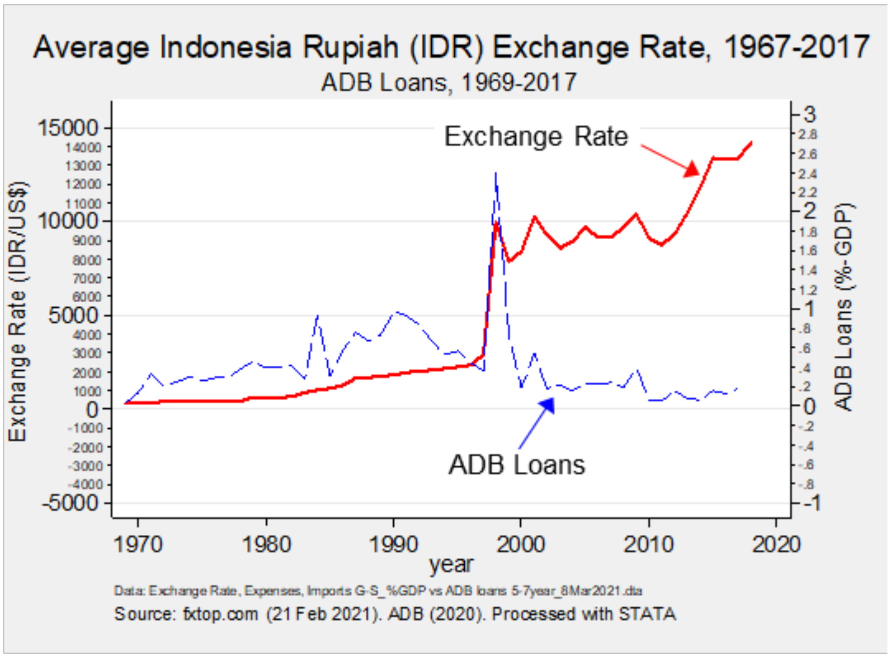


Figure 1. Indonesian Rupiah vs US Dollar

One of the World Bank staffers (Jarotschkin and Kraay 2016, 235) has identified a similar currency depreciation pattern as a result of development aid disbursement delays using over 100 countries' data. They establish that *"there is little evidence that aid inflows lead to significant real exchange rate appreciations"*. Their results show after 5 years of delay, for every 1%-GDP of aid, the national currency depreciates 0.5% (Jarotschkin and Kraay 2016, 236).

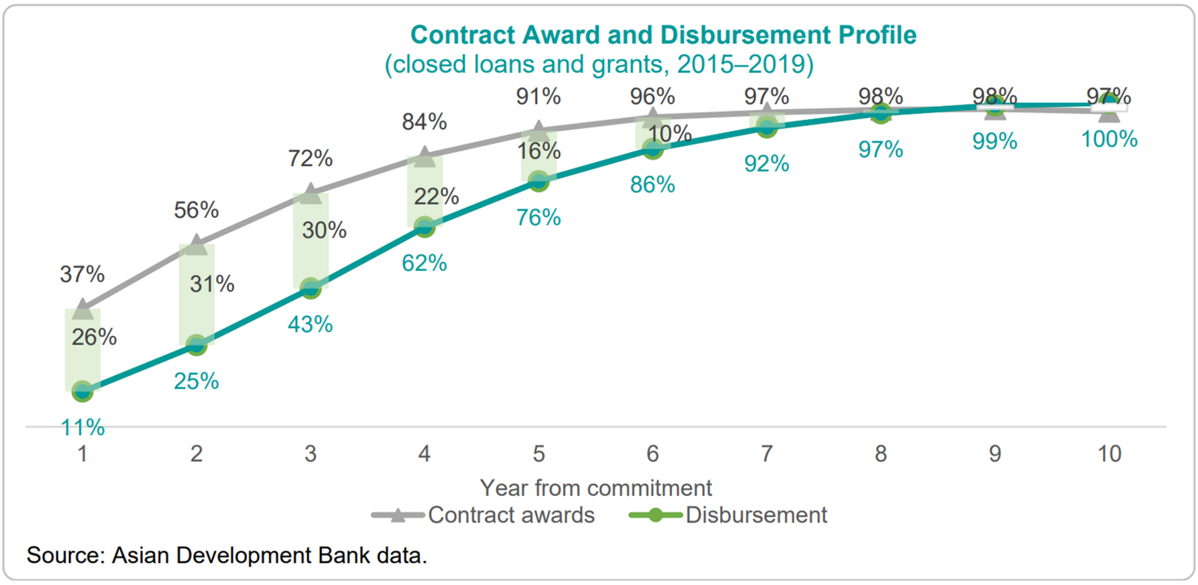
Although the depreciation shown is not entirely caused by ADB loans, we can attribute a portion thereof to them since the bulk of ADB loans to Indonesia is denominated in US dollars. Accordingly, Ingratubun *et al* (2021a) exhibit that ADB loans, had they been disbursed 100% in year-1 show stabilizing effect that holds Rupiah constant at Rp2000 per one US dollar. However, after 5-7 years of delays, ADB loans display destabilizing result in which for every 1 %-GDP of ADB loan disbursement delay, Indonesian Rupiah depreciates by about 33% which is more extreme than Jarotschkin and Kraay (2016) finding.

Money purchasing power depreciation and/or inflation is another form of non-transparent taxation that is subject to the Laffer curve (Fields 2020, 14) and a capital loss (Paliwala 2020) which Indonesia has been paying since 1967 with its ever-depreciating Rupiah. The Laffer curve has its origin from Ibnu Khaldun's work (Khaldun 1377, 352) which hints that the end of a dynasty is marked with ever-increasing taxes.

I argue that currency depreciation is another form of rent or non-transparent taxes for being integrated into world capitalism as their satellite (Frank 1989). This shows that Indonesia has been obtruded with Dutch disease, working in reverse, since joining ADB. I call this a *Dutch Curse* because historically the Dutch were reluctant to let go of Indonesia as its cash-cow colony and imposed on several incomprehensible conditions during power transfer negotiations post-1945 of Indonesia's declaration of independence. One of which for Indonesia to pay off their (the Dutch) debts of about $1.13 billion in 1949 during and after

300-year colonizing Indonesia (Isnaeni 2010). Strangely, Indonesia agreed. The Netherlands is one of the shareholders of the ADB.

Indonesia endures capital loss in form of outflows, not only during Dutch colonialization but also from borrowing from the ADB (Fauzi and Ingratubun 2020). This is because of its infamous disbursement delays that could take more than 7-years (Figure 2) before disbursing the debt funds into the economy of Indonesia, which in most cases are not 100%. For comparison, commercial banks take only 35 minutes (Werner 2014, 14). A study by the Organization for Economic Co-operation and Development (OECD 2003) discovered that disbursement delays are one of the five most burdensome donor practices that may cause aid ineffectiveness. Diarra (2011, 7) has empirically identified that the *"disbursement delays approach"* by donors is one of the principal causes of aid volatility despite some studies show different results (See Diarra 2011, 2, footnote 4). The Lowy Institute (2017) reported that*" the ADB has been criticised for being too slow and bureaucratic, and for not adequately addressing the needs of its clients."*



Source: Figure 16, ADB Annual Portfolio Performance Report (APPR) 2019

Figure 2. ADB Actual Disbursements

The main reason for Indonesia's borrowing from the ADB is to help the government's intervention, for promoting growth and trade. ADB's official mission is poverty eradication in the Asia and Pacific region. Gann and Duignan (1979, 30) argue that following the example of the Dutch in Indonesia, King Leopold of Belgium philosophy in Congo was that *"the colonies should be exploited, not by the operation of a market economy, but by state intervention ..."* The ADB was established to provide its members with resources for their state interventions in developing their economies. However, this comes with conditionalities.

At this point, I am intrigued to see Indonesia's economic development performance (Figure-3) compared with ADB overall loans impacts to Indonesia (Figure 4). These figures were plotted using fractional polynomial regression with STATA software. I opted for this regression as both their Akaike (AIC) and Bayesian (BIC) Information Criteria are much smaller compared with the regressions (i.e., linear, smoother polynomial, and quadratic). Smaller AIC and/or BIC suggest that the result is more accurate. I used public data provided by the World Bank (2020) and ADB (2020). From these 2 figures, we see that ADB loans are performing worse than Indonesia's national development. If we look closely at the poverty alleviation chart, Indonesia is performing extraordinarily well reducing poverty from about 90% to around 10% as the current GDP increases annually. On the contrary, ADB loans worsen Indonesia's poverty as their values (%-GDP) increase relative to Indonesia's GDP from around 5% to 70%. These figures serve as evidence that Dutch Curse is busy at work making Indonesian poorer through ADB loans.

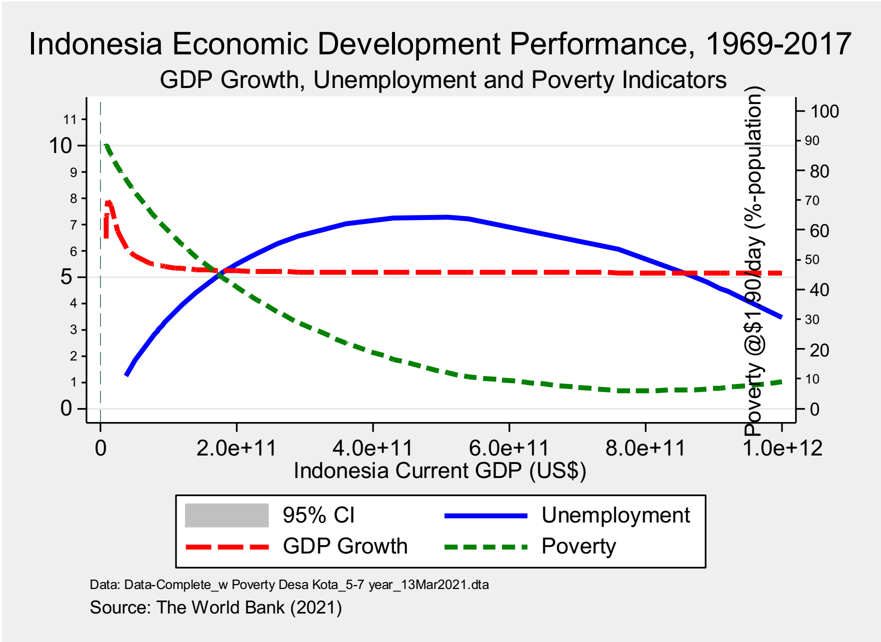


Figure 3. Indonesia Development Indicators

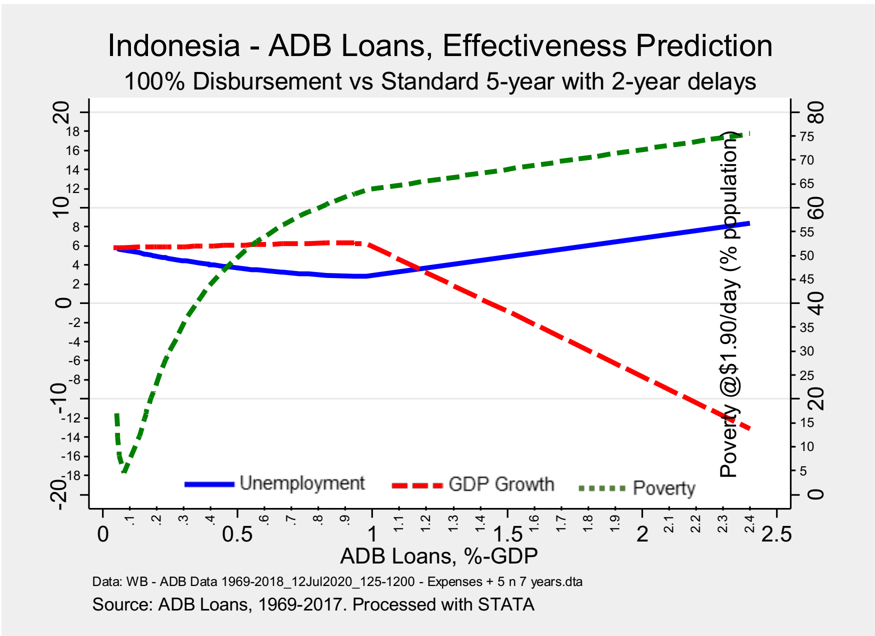


Figure 4. Indonesia-ADB Loans Negative Impacts

Indonesia's poverty has a long history most notably because of over 300 years of Dutch colonization which ended in 1945. Since then, Indonesia has been fighting to eradicate poverty including joining the ADB in 1966. Ingratubun *et al.* (2021b) share their empirical observations on ADB's disbursement delays that because of them the energy poverty begets more poverty in various forms. Not only in the form of deteriorating poverty, but also negative growth (Fauzi and

Ingratubun, 2020), and increased joblessness (Cahyadie *et al*. 2021). Zonday (2018) expresses this as *"poverty charges interest"*.

Bryant (ed. 2015, 182) states the arguments by certain capitalists that resource curse (or Dutch disease) is a mechanism in which more money for the local authority will only produce more poverty hence they argue those monies should be better managed by corporations (or quasi-government-quasi-corporation, such as ADB since it has shareholders) than by the local or national governments. This is similarly reasoned by the development partners, including the ADB, as one justification for withholding aid disbursements with the chief arguments that the recipients are lacking capacity, despite contrary evidence that shows Indonesia has about 200 times larger disbursement capacity than ADB (Cahyadie *et al*, 2021, 7). In ADB loans case, they hold the loan money by delaying disbursements. This is like Wolf's description of denied access to labor products. Hence the *Dutch Curse* is infecting Indonesia.

My findings, as exhibited in Figure 3 and 4, show Indonesia's ADB loans, instead of increasing growth, retard and reduce it to negative. Despite initially reduced unemployment until at 1%-GDP, beyond this ADB loans, as they increase, constantly heighten unemployment level. Likewise, poverty is worsened instead of reduced which is contrary to ADB official rhetoric and published mission of poverty eradication.

Establishment of ADB

The planning and establishment of the ADB was about the same time World War 2 and decolonization ended between the 1940s-1960s. ADB adopts ***'one Dollar one vote'***. Japan and the US combined hold 31.142% of the voting power. Japan is the largest holder ($1.3 trillion) of US Treasury securities thus it is the reason to provide relentless support to the US commercial interests in ADB operations. Hudson (2003, 239-240) elaborates that in 1969, the US approached its bilateralism through the appearance of multilateral development, which was in fact *"[a] predominantly bilateral United States program"*, to lessen domestic opposition. This is part of the US tactic recommended by Congress in 1957 in using Japan and other nations' resources for burden-sharing in supporting US geopolitical and commercial interests.

The US Congress (1968a, 280) record on the US and its allies' investment in ADB registers that *"we find that many of the members… put in $1 and get out $7 [or 700%]."* Furthermore, *"[w]hen the Japanese parliament was supposed to vote for the US-Japan Security Treaty in the 1960s, continuing US occupation, all opposition parliamentarians were arrested by the police… Then "majority" approved."* (Werner 2020). Subsequently, Calder (1988) discovered evidence of *"gaiatsu"* described as a Japanese policy as a reaction to US pressure in transmitting aid flows across borders and regions, in exchange for safeguarding the security and interests of Japanese multinational firms and US market access. This appears as a conflict of interests (COI).

Conflict of interest (COI) in ADB

Kilby (2006, 2011) shared that since ADB's establishment, it has been criticized for COI as its two main shareholders, Japan and the United States (US), have more strategic influence over lending, policy, and staffing decisions (citing Krasner, 1981). The president of the World must be American and Japanese citizen for the ADB (Kilby 2006). Kilby finds evidence that is quantitatively and statistically significant that the US and Japan have a strong influence on ADB's disbursement rates (Kilby 2011, 227) and questions their relative merits on economic grounds (Kilby 2006 3). Albeit COI is akin to corruption (ADB 2008, xiii), Chavez (2002) expresses that ADB is not doing what it preaches on integrity and COIs as *"There are just too many elements of the governance principle that threaten the very foundations of the Bank."*

ADB supervisory, terms as fiduciary, roles present both appearances of conflicting interest whereby it controls the flow of disbursement through its No-Objection (NO) procedures, in which ADB's approvals have to be obtained before making any progress. Borrowers can opt to proceed without ADB's NO and later apply for reimbursement while risking being refused funding for the corresponding action. If ADB objects part of- or fully the Withdrawal Application (WA), the amount claimed will not be paid and kept under ADB's control. During which, the loan fund creates multiple-folds money under fractional reserve banking practices or money multiplier (Nichols, 1994 revision, 11, 1st Published in 1961), earns compounded interests and commitment fees (min 0.15% (15 bps)) for ADB or whoever holds the funds (commercial banks) on its behalf. This explains, despite rhetoric and narratives of reducing implementation delays, yet it persists since its establishment in 1966 of about 2 years delays (US Congress, 1968a, 274; 1968b, 25-26 and Ministry of Finance, Republic Indonesia - MOF-RI data 2020).

This exhibit, on one hand, a conflict with temporal values of money in which money, where it stays invested in the bank or flows out into the economy, generating additional benefits such as raising income, creating jobs or reducing unemployment, poverty alleviation, and stimulating economic growth among others. On the other hand, US Government's record (1968a, 274) disclosed that ADB is earning interest from commercial banks on their time deposit.

Indonesia's paid-in (in-cash), subscribed capitals, and guarantees (in-kind) to ADB which under banking practices are categorized as Promissory Notes (PNs) following Bill of Exchange 1882 thus can be traded as securities or leveraged to create money. Each signed LA is a tradable security and bank reserve (Nichols 1994, 11; Werner 2016 and IMF 2019) and adding to Indonesia's securities to ADB. These can be used as 100% full loan-fund-disbursement collateral. Despite this and Indonesia's much larger disbursement capacity, ADB is asserting on controlling the disbursement and strangely GOI agrees. Hence, for Indonesia's national development planning, Rodney (1973, 33) reminds us of being underdeveloped, that; *"Power is the ultimate determinant in human society... When one society finds itself forced to relinquish power entirely to another society, that in itself is a form of underdevelopment."*

ADB insists on following its interpretation of its Charter, Article 14 to ensure that they used loan proceeds for eligible items and their intended purposes. However, this practice presents the appearance of- and/or real COI which ADB defines as *"any situation in which a party has interests that could improperly influence that party's performance of official duties…"* (ADB's Integrity Principles and Guidelines 2015, 6). *"A situation that appears to be a conflict of interest may be enough to undermine public confidence, even if an actual conflict does not exist…"* (ADB 2008, 6). The test is, ***'who is benefited from ADB's disbursement delays?'*** The longer the fund is undisbursed, the bigger commitment fees the borrower has to pay to ADB while it profits from compounded interest and fees on the undisbursed amounts.

OECD (2007) defines a COI *"occurs when an individual or a corporation (either private or governmental) is in a position to exploit his or their own professional or official capacity in some way for personal or corporate benefit."*

Hancock (2009, 2) posits that the designer of international agencies, the like of ADB, such as the US and Japan do not delegate the policy-making to other bodies or representatives. They simply hold the veto power often cloaked with their voting policy that was purposely designed for favoring them. By controlling the policy-making, the entire region under the guise of regional integration, the designer or the majority shareholders are benefiting their constituents which mostly the developed countries. She reiterates this *"[u]nder plutocracy, only the Designer enjoys veto power. Second, the Designer now controls policy for the entire integration area. This allows the Designer to more fully benefit its winning coalition."* (Hancock 2009, 48)

The COI causes a capital flight of 4.98%-GDP from Indonesia's total loans from ADB which is almost double the expected return of 700% per $1 (2.91%-GDP) by developed member countries in their investment in ADB (US Congress 1968a, 280). The evidence to date shows that ADB loan volatility through disbursement delays is not incidental. On the same tone, Hayter (1971) argues similar practices are imperialism in disguise and cannot result in any meaningful economic benefits. If any at all, it would only be incidental and not planned. Rostow (1960, 102) considers foreign assistance, which he refers to as pre-conditions fathered by colonialism, and their conditionalities as the *"external intrusion by more advanced societies"* as the price, rent, or tax the developing country has to pay for their membership in the international arena (Frank 1989). Acemoglu *et al*. (2001) attribute this as economic retardation in less developed countries (former colonies) because of the creation of extractive institutions. *"The main purpose of the extractive state was to transfer as much of the resources of the colony to the colonizer, with the minimum amount of investment possible"* (Acemoglu *et al*. 2001, 2). Hence, for Indonesia, the Dutch Curse is well at work.

ADB Disbursement Delays in Indonesia

> *Aid disbursement delays, however defined, constitute a significant worldwide problem… It was therefore surprising to discover, once again, that there appear to be no clearly defined and generally accepted ways of measuring this problem. In addition, there appears to be no systematically collected and recorded data on this subject.* (Leurs 2015, 380)

Development banks, such as the ADB, operate in similar ways to traditional banks (Mazzi 2013, xxvi). However, unlike borrowing from a commercial bank where the fund or bank credit disbursement in full and deposited into the borrower-controlled account upon Loan Agreement (LA) signing, borrowing from ADB does not work like this (Figure 2). The ADB ties its disbursements with certain conditionalities and controls the loan account. Kanbur (2000, 413-416), a former World Bank staffer, expresses that conditionality of whatever type has failed in Africa and they designed it to fail as a systemic imperative to ensure the aid keeps flowing. Conditionality incriminates the actual issue that is "*one of an unhealthy interaction between donor and recipient processes which propagate aid dependence but are not so simple as to be characterized as the strength of the donors and the weakness of the recipients*" (Kanbur 2000, 414). This is similar to the subordination observed by Biersack (2006). To date, as shown by Howarth (2017, 33) that the infliction of conditionality is a nuisance, highly controversial, and ineffective.

Leurs (2005, 381) expresses that *" [t]he importance of disbursement delays is reflected in their consequences"*. Ingratubun *et al.* (2021b), exhibit ADB energy loans cause about a 300% increase in energy poverty in Indonesia because of fund control through disbursement delays. The controlling or withholding of the loan funds appears to stem from questionable intentions. One of which as described by a former US Senator Pettigrew (1922, 50-51);

"How conscientiously this control over money has been exercised is indicated by the actions and utterances of the bankers themselves.…

In 1862, the creditors of the United States, the Bank of England, sent the following circular to every bank in New York and New England:

> ***Slavery*** *is… I and my European friends are in favor of, for slavery is but the owning of labor and carries with it the care for the laborer, while the European plan, led on by England, is for capital to control labor by controlling the wages.* ***THIS CAN BE DONE BY CONTROLLING THE MONEY.*** *The great debt that capitalists will see to it is made out of the war must be used as a means to* ***control the volume of money****. To accomplish this, the bonds must be used as a banking basis."* (Emphasized)

This evidence should prepare us to see the negative impacts of disbursement delays as means of money control not only by the ADB but also other development partners.

Browne (2006) expresses that once one understands the real objective of the donors that are not entirely for development works, they claim to deliver, how one measures their effectiveness will be largely affected. He stresses that *"[i]ndeed, where aid is allocated mainly for the 'wrong' purposes, it may be better to hope for failure."* This brings us to the question of morality as defined by the Cambridge Dictionary and makes us ponder about the quality of being right and honest of both the Government of Indonesia (GOI) and ADB as its development partner. This includes the truthiness about their publications on the ADB loans operation results and outcomes.

Teresa Hayter (2009 as cited by Baird) who wrote the book *"Aid as Imperialism"* in her response to the New Internationalist magazine argues that aid, in whatever form they are delivered, with the impression that they are intended for poverty alleviation, cannot be believed. She further elaborates that, after a long and slow investigation she reached the painful conclusion. That it is not a conspiracy theory *"some aid projects may be beneficial but others not. "… above all, the policies which governments have to adopt to get the (aid) money are deeply damaging to the interests of the poor. I believe, therefore, that official government aid, on balance, does more harm than good to the poor of the Third World."*

Recommendation

In fixing the issue of lack of funding for economic development, it should make us ponder what Keynes (1933, 756) eloquently expresses *"above all, let finance be primarily national"* in his lecture on self-reliance. Or perhaps no ADB loans at all and maximize national funding sources.

Conclusion

As ADB loans appear worsening Indonesia's economic development indicators while at the same time leaving the traces of Dutch Curse fingerprints that is busy at work since early 1600s, one should carefully examine the ADB official rhetoric and published narratives as Lord Acton expresses *"Official truth is not actual truth."*

Given the negative evidence exhibited, it is hard not to question the morality and demand the responsibility and conscious awareness of both the government of Indonesia (GOI), and ADB who provides the US dollar denominated loan financing, for its externally funded development programs.

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