Research Article

Political Economy and Ecology of International Regional Development: Indonesia Urban and Rural Development Loans from the Asian Development Bank (ADB)

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We reviewed the political economy (history) of development aid and its political economy (unequal exchange or plunder). We adopted a combination of theory deconstruction, reconstruction, and empirical testing. We plotted the results by harnessing fractional polynomial regression and charting. Applying political economy, we deconstructed the foundation of development economics theory of exogenous growth (EXGT) and savings-investment gap (SIGT) theories. We discovered that these theories are false and faulty. Endogenous growth theory (ENGT) which holds that economic growth is predominantly the result of endogenous and not external forces is the prevailing theory supported by credit creation banking and finance theories and practices. This is also known as endogenous money. After reconstructing the correct theories, and applying them in our empirical analysis, we adopted political ecology, also known as imperialist rent, to estimate the capital outflow as a percentage of the loan compared with the actual disbursed amount into Indonesia. We observed their ramifications on Indonesia's Rupiah exchange rates and imports. We witnessed that external financing through foreign currency borrowing is unnecessary. Each country can source and create the funding themselves per international banking laws. These laws also govern that not a single cent of foreign currency debt ever enters the national economy of the borrowers hence external borrowing is not required. When Indonesia borrows in foreign currency, it becomes the lender to their bankers or creditors when it demands payment in Rupiah. We discovered that only about 2% of ADB loans are disbursed in Rupiah in Indonesia. This yields 98% capital flight. ADB loans and their disbursement delays (DDs) governance caused a deterioration of the Rupiah of 33% for each 1% of

 doi.org/10.32388/LJIEWJ

GDP of ADB loans. They increased imports as ADB loan gets bigger and DDs causing Rupiah to further deteriorates 200% faster.

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1. Introduction

The creation of International Regional Development Organizations (IRDOs), like of the United Nations (UN), World Bank, International Monetary Fund (IMF), including the ADB, took place in the post-World War 2 and decolonisation period. ADB adopts 'one Dollar one vote'. The controlling shares are owned by European-origin countries, most of which are former colonial power. Japan and the United States (U.S.) of America combined, hold the controlling voting power. This strategy was proposed by Congress to create U.S. bilateralism through the appearance of 'multilateral development' (1). The focus of the IRDOs is to unite the world under one governance system using financing as the primary vehicle. For this, theories must be developed to justify any international—including regional—initiatives.

Development aid (aid)[1] was born inexplicably coinciding with the end of the decolonisation period in the 1940s. The introduction of development economics and econometrics and their propagations both through academic curricula and operational instauration for the IRDOs accompanying its birth. The underlying theory is known as exogenous growth theory (EXGT) wherein external assistance in all forms, mostly in financial aid, is necessary for the development of the newly independent states into developing countries' status. The EXGT is coupled with the savings-investment gap theory (SIGT) in which national savings are said to be inadequate to provide funding for the domestic economic development agendas, thus external borrowing—which is also purported to come from savings—is needed. SIGT then became the foundation for developing countries to borrow externally for financing their development agenda. These theories become the cornerstone of the *Washington Consensus* for developing countries' development financing liberalisation, regulatory reformation and deregulation, and market privatisation.

However, these theories are faulty.

1.1. *Purpose*

ADB was established for addressing the issues of economic development and poverty eradication through regional development cooperation and integration in mobilising development funds into the Asia-Pacific Region and their borrowers' economy. We investigate whether empirical data supported this or if they implement different agenda. We explore this by looking at development aid underlying theories (i.e., EXGT and SIGT) and ADB's disbursement governance (DG). We suspected that something is not right with development economic theory as a myriad of studies despite 100 years of aid history, remains inconclusive [1][2]. We argue that ADB's DG is one of the underdevelopment tools —defined as dependency tethering (or being controlled) and looting [[3], p. 274] by Western countries' capitalists and former colonisers. Disbursement Delays (DDs) have been studied by many authors with unfavourable results for borrowing countries ([4][5][6][7]). Our paper focuses on the actual foreign currency loans (FCLs) from ADB that are actually entering Indonesia's banking systems and national economy. How much of Indonesia's loans from the ADB that actually disbursed into its national economy? From this point on, we define capital flights as FCLs and/or Foreign Direct Investments (FDIs) that are committed through legal agreements but never enter or have entered but exported for other than funding national development. Political ecology termed this as unequal exchange [8][9], plunder [10], colonial or imperialist rent [11], exorbitant profit and rent-seeking [12].

1.2. *Potential Contribution*

The theory on FDI, FCLs, Overseas Development Assistance (ODA), and their disbursement governance need revamping as recent country-studies evidence including from the IMF [13] suggests they are not inducing growth [14]. In reality—as stated in the U.S. Central Bank (The Fed) publication —they have no impact in their foreign currency form on the borrower's economy [[15], p. 28] unless they are converted into the national currency [[16], pp. 375-376]. The IMF has similar results [13]. This makes the borrower becomes the national currency lender to their foreign currency lender [16][17]. The understanding of which will have ramifications in not only academic textbooks but also national development policies particularly in the external borrowings, among others.

doi.org/10.32388/LJIEWJ

2. Methodology

2.1. Method

Our methodology is a combination of theory deconstruction, reconstruction and empirical testing. We plotted the results by harnessing fractional polynomial regression and charting with the assistance of STATA[2].

Applying the political economy (or history) of development economics, we deconstructed EXGT and SIGT and discovered that these theories are faulty. We adopted endogenous growth theory (ENGT) which holds that economic growth is predominantly the result of endogenous and not external forces [18][19][20][21]. Complementing this, we observed numerous study results—particularly those in the last ten years with numerical evidence on the benefits and impacts of FDIs and development aid loans as external sources of financing for developing countries. These have debunked EXGT and proven that it is a false theory [13][14][16][22][23][24][25][26][27][28][29]. Additionally, we embraced modern banking, debt and finance theory (BDFT) since1800s in tandem with empirical evidence and live banking practice testing witnessed by BBC film grew, both of which established that SIGT is faulty [29]. Following this, we adopted political ecology or known as unequal exchange [8][30] or plunder [10] to estimate the capital outflow as the result of Indonesia's borrowing from the ADB.

The modern banking theory empirical test by [29] has proven that no countries need external financing as they can source and create the funding themselves per international banking laws which govern that not a single cent of foreign currency debt ever enters the national economy of the borrowers. When reading this foregoing statement, one needs to bear in mind the difference between tangible external aid such as wheat, rice, or pieces of machinery, and financing which is not tangible, such as FCLs, as they are only numbers entered by the banker through computer keyboard as explicitly stated by Bank of England [31]. Also, the borrower becomes the lender to their bankers or creditors when they demand payment in their national currency [16]. Accordingly, there is no need to borrow money in foreign currency [14][15][16]. Furthermore, the faulty SIGT is present in most textbooks, widely taught at secondary schools and universities around the world thus becoming common knowledge. Most notably, it is present in all central banking laws in most countries around the world, regarding how banks work and create their money for investment. Following this, we reconstructed the theory and applied them in our empirical analysis.

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2.2. *Data*

We harnessed data available online from, among others, the ADB, World Bank, and the Indonesia Ministry of Finance. We reviewed Indonesia's loans (regional, urban and rural development) from ADB since 1969, totalling over $33 billion (average 0.42% of GDP). Given the page limit, we look at some length into the political economy and political ecology of ADB loans to Indonesia. We focus on what actually disbursed into Indonesia's economy.

3. Results and Discussion

3.1. *Political Economy – International Regional Development*

The history of all IRDOs including the MDBs of which ADB is a member, seems to have its roots, governance, and operational structures with the Dutch East India Company or *The Vereenigde Oostindische Compagnie* (VOC) in Indonesia. What many do not know, the VOC was a bank. The Dutch government, like all former colonial masters, was not happy about Indonesia—as their cash cow—gaining its independence. To this day, their Queen/King does not publicly recognise Indonesia's independence. The VOC's structure and holdings are echoed by the UN and MDBs. This indicates a strong colonial connection with the IRDOs. Hudson [32] argues that in 1969, the United States pursued its bilateralism through the appearance of multilateral development, which was in reality a predominantly bilateral program by the United States, to reduce domestic opposition by the recipients. This is part of the U.S. tactic recommended by Congress in 1957 of using the resources of Japan and other nations to share the burden of supporting the U.S. geopolitical and commercial interests. The U.S. Congressional [33] record on the U.S. and allied investments in the ADB states that *"we find that many of the members... put in $1 and get out $*7 [or 700%]*."* Calder [34] discovered evidence of *"gaiatsu",* a Japanese policy describes as a response to U.S. pressure in routing aid flows across borders and regions, in return for the security and interests of Japanese multinational corporations and access to the U.S. market. Kilby [35] empirically found that ADB practiced Conflicts Of Interest (COI) wherein the developed country members dominated by Japan and the U.S. employ ADB for their geopolitical agenda.

Driver [36] argues that *The Marshall Plan* is the best example of development aid propaganda. The main goal of this plan was to help U.S. companies to capture overseas markets for their export products[3].

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Regional expansion, economic integration, and control under the guise of cooperation are the hallmarks of colonisation and also of development aid. Werner [37] calls this a 70-year practice of neo-colonisation. Therefore, we argue that the establishment of the ADB under the guise of regional cooperation, development work, and/or integration follows the pattern of neo-colonialism. Hayter [38] as cited by Baird [39] plainly expresses that (emphasized):

> *"[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.****"*

The evidence shows that ADB loan volatility is caused by DDs which is justified by ADB (also MDBs) by stating that the borrower (Indonesia) lacks disbursement capacity. However, MOF-RI (2020) data indicates that Indonesia has a disbursement capacity of over 220% [40] compared to the ADB. This appears to have been planned and intentionally implemented on the instructions of European bankers to keep the colony permanently in sustainable poverty, unemployment, and slavery [41][42] on the Hazzard (Banker) Circular. This is one of the two reasons for arguing that ADB (and MDBs) loans are not beneficial to Indonesia. The other reason is the flawed EXGT and the false SIGT debunked by the Endogenous Growth Theory (ENGT) and Endogenous Money (EM) [27] or Credit Creation (CC) [16] of banking theory and practices, which show that each nation can create its own (endogenous) sources of capital, including money without relying on foreign (exogenous) financing. Keynes postulated this prior to the establishment of the MDBs in 1933 [43]. Thus, for almost all (if not all) financing needs of economic development, there is no need to borrow from abroad.

3.2. Political Ecology (Plunder)

3.2.1. Aid Benefits Rich Countries More Than Poor Countries (Backwash Effect)

Driver [36] cites the U.S. government agency (USAID)4 noting that *"The principal beneficiary of America's foreign assistance* [including ADB's U.S. Dollar loans] *has always been the United States."* Hickel [44] examines the unequal exchange and finds that poor countries export capital to rich countries over $ 2 trillion per year or $24 ($30, [45]) for each $1 aid. **Our result shows an average of $34 per $1 of ADB loans**. Our finding suggests at least that 4.98% of GDP goes into capital flights from ADB DDs alone. Moreover, the range is from 14% (for GDP transaction) to 190% (endogenized) of Indonesia's GDP in capital flights or plunder due to ADB loans including the MDBs. Subsequently, it

doi.org/10.32388/LJIEWJ

was reported that *"aid resources are...often misdirected. They are increasingly being deployed in ways that exacerbate rather than eradicate poverty."*[5] Hickel [44] argues that the development narrative is backward. **It is poor (developing) countries that develop rich (developed) countries.** Myrdal [9] sees this as a backwash effect, which is a negative consequence of poor development planning.

3.2.2. Faulty Development Theories (The Myth of Savings-Investments Gaps)

> *"Beware of false knowledge; it is more dangerous than ignorance..."* ~ George Bernard Shaw

Development economics and econometrics were born, curiously, at the same time that decolonisation ended in the 1940s. This was followed by the creation of the IRDOs and Multilateral Development Banks (MDBs) including ADB in 1966. The underlying theory was developed separately by Harrod [46] and Domar [47] and is known as the Harrod—Domar theory of exogenous growth (EXGT), later extended by Rostow in the 1950s as linear growth stages inspired by Karl Marx and Friedrich List works. Rostow expanded Marx's development theory to focus on capital accumulation through domestic and international savings as the sources of investment to promote economic development and growth. Solow–Swan further developed this model relying on the golden rule of the saving ratio which is an equilibrium between the capital and production ratios that depends solely on the saving ratio for the investment to promote growth. Thus, the savings-investment gap is the theoretical basis for all development policies. However, this theory is flawed because it does not take into account the role of banks, finance, and debt [14]. The evidence gathered shows that savings are not required to invest. As shown by the prevalent banking practices, the required funding can be generated by any economy without depending on external sources. This was confirmed by Keynes [43] who prescribes in his lecture on self-reliance that *"above all, let finance be primarily national"*.

Robert B. Anderson, Secretary of the Treasury [Finance Minister] under President Eisenhower, expressed in 1959 that banks do not need prior savings to make loans or investments. They simply create the money. The Bank of England and the International Monetary Fund (IMF) confirm and explain this (emphasized):

> ***"New funds are produced only with new bank loans*** *... through book entries* ***made by keystrokes on the banker's keyboard at the time of disbursement.*** *This means that* ***the funds do not exist*** [no prior savings] *before the loan* [investment] *and that they are* ***in the form of electronic entries ... rather than real resources."*** [48]

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The IMF [[49], p. 23] substantiates Werner's empirical finding [29] and concludes that their empirical result (emphasized) *"do not negate the fact that* ***banks create ... money "out of nothing"*** *upon the* ***creation of loans****."* In other words, the loan that the ADB provides to Indonesia is created out of nothing, using the loan agreement signed by Indonesia's government after surrendering certain collateral (endogenous capital) which is larger than requested by the commercial banks.

So, what does the bank do? Hyman Minsky answers (emphasized); ***"Banking is not money lending****; to lend, a money lender must have money."* [50]. This was later confirmed by the IMF and Bank of England [48] whose publication was commented on by Graeber [51] (emphasized), "*[i] n other words,* ***everything we know is not just wrong–it's backward****. When banks make loans, they create money."* It is clear from the Central Bankers' admission, that money lent by the banks (including ADB) is not prior savings exchanged and traded with the borrower's assets, real resources, and sovereignty. The money does not come from deposits or savings negating SIGT (from Harrod-Domar to Solow-Swan and Cobb-Douglass). Most authors have not considered banks, finance, and money in their studies [14][29][40][27][52]. From this, we can safely conclude that they built previous development theories and work **on flawed or incorrect theories**. We can now anticipate the negative effects of any foreign currencies loans (including from ADB), whether they are supposedly cheaper—which is not the case (see above)—or whether their seemingly noble reasons of poverty alleviation—which is not the case [53]— as Myrdal [9] postulated in his theory of cumulative causation that peripheral regions—which denotes developing countries—is suffering the most evidenced by the poverty prevalence. It is poor countries that develop rich countries [44]. Myrdal labels this spread effect.

3.2.3. Foreign Currency Borrowing – Never Enters National Economy

Current banking practice requires that the borrower surrenders his assets, in the form of a loan agreement (LA) which is a financial instrument called the Promissory Note. As a result, Werner [16] argues that there is no need to borrow in foreign currency because the money never enters the national economy. He claims that this practice is a *"cruel trick"* for poor developing countries. This has been confirmed by the U.S. central bank—and many other authors, which were listed in the IMF publication [49]—the Federal Reserve Bank (The Fed) since 1961, thus before the creation of the ADB in 1966 (emphasized): *"The key point to remember, ...* ***foreign-related transactions... do not affect money and credit growth in the United States*** [or Indonesia]*".* The US Central Bank, [15]. 1st edition 1961.

3.2.4. Capital Flights and Regional Transfer (TKDD)

Indonesia suffers a capital flight of at least 4.98% of GDP from Indonesia's total loans from ADB [40] which is almost doubled the expected return of 700% per $1 (2.91% of Indonesia's GDP) that developed member countries expect for their investment in ADB [33]. Hickel *et al.* [10] show that Indonesia suffers 3% of GDP in losses or unequal exchange. In essence, after completing the project[6] (2010-2014), Indonesia suffered a backwash effect [9] of over $260 million from an $84 million loan after the project completion (2010-2014), while it could have benefited from capital creation (Myrdal's spread effect, [9]) of nearly $98 million over a 20 years loan term if Indonesia had borrowed from domestic banks. We found that only about 5.35% (2004-2017) and 7.05% (1969-2017) respectively of Indonesia's foreign currency loans are drawn annually (MOF, 2022; Bank Indonesia, 2022). From this, we uncover that only 2.12% of the ADB annual disbursement reached Indonesia's economy after we converted them into Rupiah (See **Figures 1 and 2**). This means about 98% of capital flights annually from ADB loans.

A Nobel laureate and economics Professor, Jeffrey Sachs[7], has calculated that of the $3 per person U.S. grant in sub-Saharan Africa, only 6 cents (or 2%) was received by the people after subtracting the shares of U.S. consultants, food and other emergency aid, administrative costs, and debt relief. (See also Hayter [38]) on subsidising the West's private firms and banks). This means that 98% (excluding interests and money creation) is capital flights. Indonesia received only 1.18% (over 98% capital flights) of its total foreign currency loans compared with 2,12% from ADB loans annually. From this about zero Rupiah is transferred to the region. On the contrary, Bank Indonesia (BI) (2022) data shows about 30% is passed on to the regions if funds are sourced domestically.

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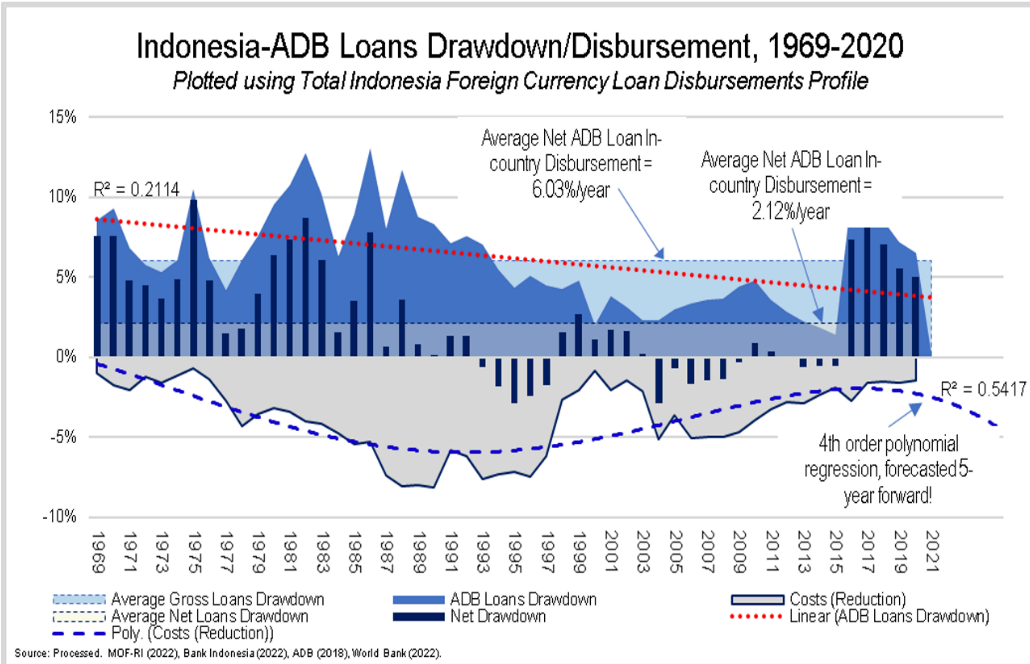

Figure 1. ADB Loans Drawdown, 1969-2020

Source: Processed

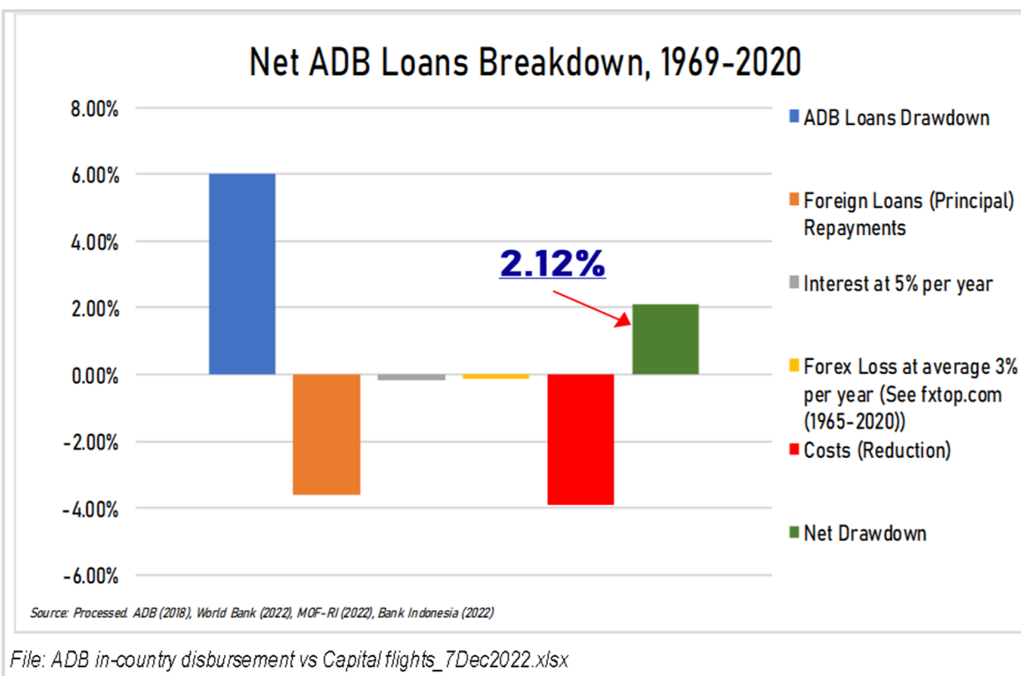

Figure 2. Net ADB Loans Drawdown, 1969-2020

Source: Processed, disbursement in Rupiah

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OECD[8] data (2021) for Indonesia's aid funds show an average of about 35%—MOF and BI's data shows about 6% is disbursed—in-country each year. After the money arrives in Indonesia, over 60% goes out through revolving doors, 3% is lost through currency exchange, and almost **zero-per cent (0%) is passed on to the provincial level**. It concerns us that OECD data shows that Indonesia has been paying more than it receives since 2005. This means that zero Dollars of all the development assistance funds are received. In other words, Indonesia suffers a negative resource transfer (backwash) [9].

3.3. Discussion

Literature suggests that regionalisation and regional development and integration were promoted by the Europeans who are all former colonisers [54][55]. The Multilateral Development Banks (MDBs) of which ADB is a member, are all controlled, mostly—if not all—by former colonisers which includes the Netherlands as Indonesia's 300 years coloniser. The UN, IMF, and MDBs, among others, are part of the IRDOs. Instead of using armies and weaponries, former colonisers adopted false development economics theories coupled with faulty BDFT and applied them as the basis for establishing the IRDOs. This causes Indonesia to suffer a capital flight known as plunder (or imperialist rent) of over $12 per $1 loan [5] or about 4.98% of Indonesia's GDP, also termed as unequal exchange. About 98% of ADB loan funds annually do not reach Indonesia. In fact, 100% of them never enter Indonesia's economy in their foreign currency forms, unless converted into Rupiah. Furthermore, if collaterals of about 10 times the loan amount are endogenized, this results in about 50% of Indonesia's GDP as capital flights from ADB loans alone. We can translate this as if 100% of ADB loans were disbursed into Indonesia's economy in Rupiah, it potentially could increase its GDP by half or approximately $500 billion.

Additionally, if ADB loans are disbursed 100%—**which is not the case as foreign currency never enters Indonesia's economy**—ADB loans, engender Rupiah depreciation of a minimum of 33% per 0.5% of GDP **(Figures 3 and 4)** and correlate with increased imports of about 20% per 1.5% of GDP. ADB's DDs expedite imports increase 200% faster in tandem with Rupiah depreciation to $16,000 per 1.5% of GDP of ADB loans **(Figures 5 and 6)**. They also retard and reduce growth to negative [5], increase unemployment by about 300% [40], and constantly increase not only energy poverty [53] but also poverty (attributed to ADB loans) by over 300% [56]. This is contrary to their narratives of poverty alleviation. Nelson Mandela understood this (2005), who expresses;

"Overcoming poverty is not a task of charity, it is an act of justice. ***Like slavery and apartheid, poverty is not natural. It is man-made*** *and it can be overcome and eradicated by the actions of human beings."* (Emphasized) — Nelson Mandela's Trafalgar Square Speech in 2005.

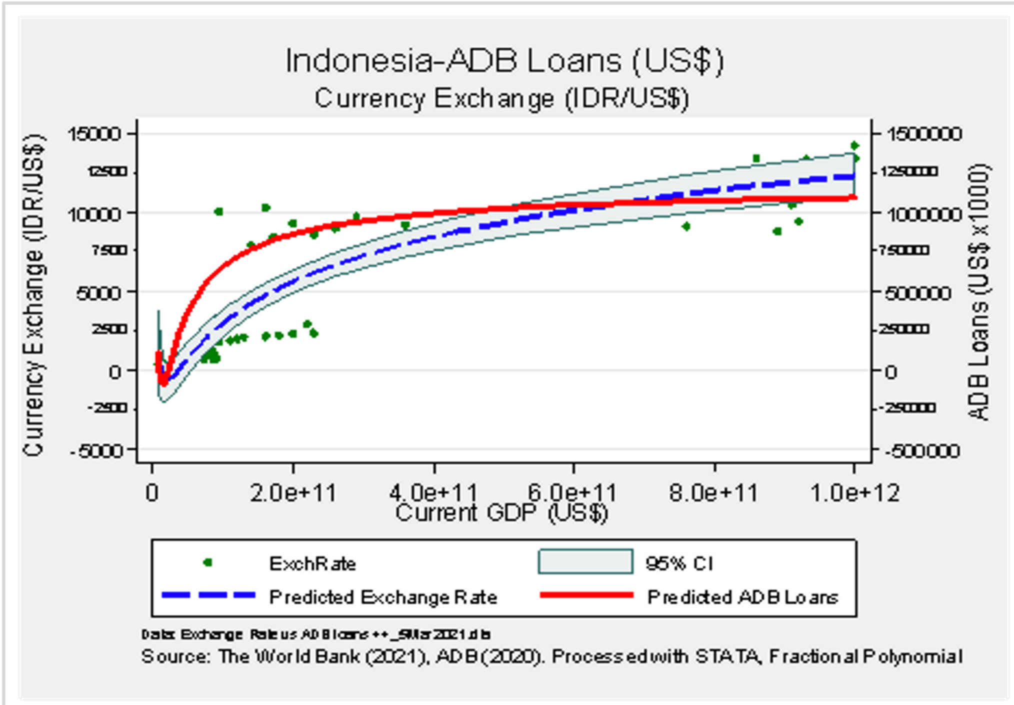

Figure 3. ADB Loans ($), 1969-2020

Source: Processed

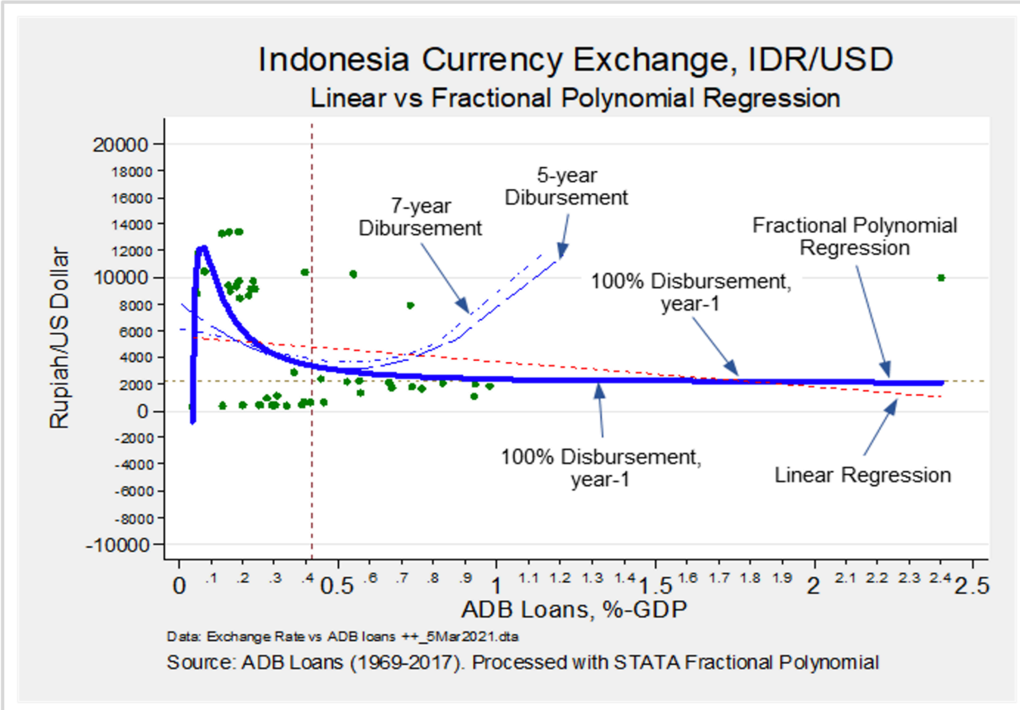

Figure 4. ADB Loans ($) Disbursement, 1969-2020

Source: Processed, assuming 100% in-country disbursement

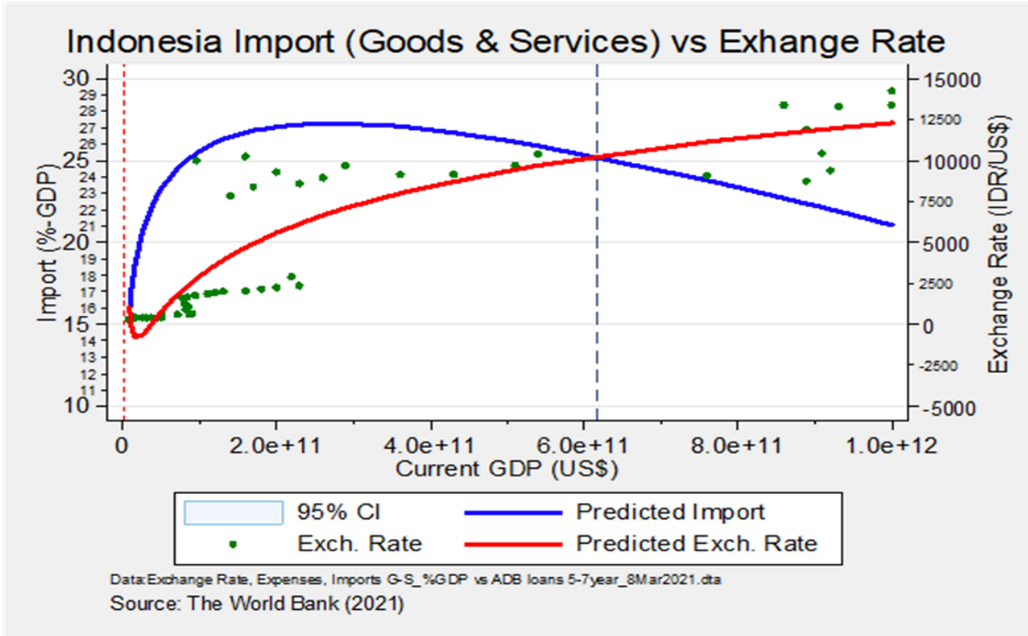

Figure 5. Indonesia Import ($) vs Exchange Rate

Source: Processed

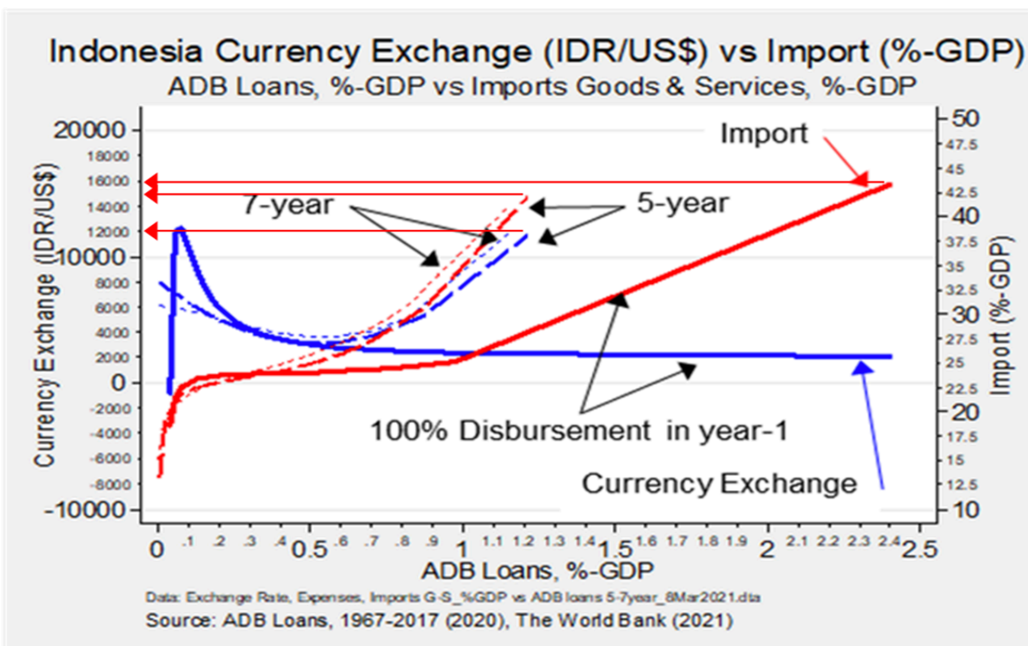

Figure 6. ADB Loans ($) vs Rupiah vs Import

Source: Processed, assuming 100% in-country disbursement

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These graphs suggest that the more ADB loans with their DG, the worse it is their impact on Indonesia.

4. Conclusions

International regional development cooperation and integration hints that colonialism through financial imperialism is still active with different facades and with US Dollar as one of its arsenals. Nonetheless, the aim remains the same which is exploitation through resource extraction [57]. Among which through capital flights. About 98% of ADB loans never reach Indonesia. The cooperation with the ADB needs to be revisited and Indonesia should demand full 100% disbursement in Rupiah immediately upon loan signing. Instead of capital mobilization from developed countries through the ADB as intended in its establishment in 1966, Indonesia suffers capital fights of at least $34 for $1 loans. Furthermore, Indonesia should urgently remedy the issue of lack of funding for economic development by implementing what Keynes [[43], p. 756] eloquently expresses *"above all, let finance be primarily national"* in his lecture on self-reliance. It appears that what he suggested was indeed endogenous money [27] that supports the ENGT.

Acknowledgements

Gratitude is extended to the Regional and Rural Development Planning of the IPB University which opens the door wider to understanding the breadth and extent of regional wealth leakages also known as the backwash effect, [9] and the tools and methods in measuring them. Most importantly for critically challenging the researchers to think without boxes.

Footnotes

[1] Aid includes loans, grants, technical assistance (TAs), and in-kind assistance (Organisation for Economic Co-operation and Development (OECD) 2021). https://data.oecd.org/oda/net-oda.htm (15 Aug 2021)

[2] Stata is a data science software by StataCorp LLC.

[3] Matt Kennard, *The Racket*, p.66

[4] USAID developments (Summer 1997) cited in '*Myth 10: More U.S. aid will help the hungry*', at https://www.globalissues.org/article/11/myth-more-us-aid-will-help-the-hungry (2 Jun 2022)

[5] *The Reality of Aid Network*, ‘RoA 2018 Report’, at https://realityofaid.org/wp-content/uploads/2018/12/RoA-Full-Report2018FINAL3-min.pdf

[6] ADB project 38385-013 Loan No. 2449: Rural Infrastructure Support to the PNPM Mandiri Project II (RIS-PNPM)

[7] Jeffery Sachs, *The End Of Poverty*, 2005

[8] See footnote 1

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Declarations

Funding: No specific funding was received for this work.

Potential competing interests: No potential competing interests to declare.