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**THE EFFECTS AND THE RELATIONS OF
FOREIGN AID:**

**A CASE STUDY OF INDONESIA AND ITS TWO LARGEST DONORS,
THE UNITED STATES AND JAPAN**

By : Mohamad Hery Saripudin

INTERNATIONAL DEVELOPMENT STUDIES

SAINT MARY'S UNIVERSITY

HALIFAX

1994



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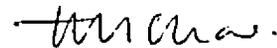
THE EFFECTS AND THE RELATIONS OF FOREIGN AID:
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THE UNITED STATES AND JAPAN

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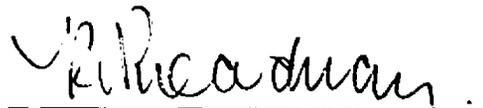
A thesis submitted in partial fulfillment
of requirement for the Master of Art degree in
International Development Studies
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Halifax, Canada

January 1994

The thesis is approved by:



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To my wife, Zulfah Nahdliyati
and my son, Faiz Novascotia Saripudin
With Love and Hope

ABSTRACT

This thesis is entitled *The Effects and the Relations of Foreign Aid: A Case Study of Indonesia and Its Two Largest Donors, the United States and Japan*. It examines the effects of foreign aid on Indonesia's political economy and patterns of aid relations between Indonesia and the U.S. and Indonesia and Japan. It is limited to foreign aid commonly defined as Official Development Assistance (ODA) in the New Order government era, especially from 1969-1991.

It reveals that the Soeharto regime benefitted from foreign aid inflows both economically and politically, and that aid has been effectively used in Indonesia for development purposes. Indonesia's economy has been growing at a steady pace. Soeharto's government has successfully utilized aid to fulfil its political purposes; Aid has deliberately been directed toward strategic sectors to disempower political opposition and maintain the status quo.

The practice of aid relations is based upon the mutual-benefit principle. The U.S. benefits from extending its ODA to Indonesia by maintaining Soeharto's Indonesia in its political orbit. Japan benefits from ODA to Indonesia by maintaining natural resources supplies inflows, markets for its products, and keeping its commercial interests flowing, stable, and secure.

The study predicts a different direction and tendency towards Indonesia by both the U.S. and Japan in the post Cold War era.

Halifax, January 1994

Mohamad Hery Saripudin

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Finally, needless to say, this study is far from perfect and the final responsibility for opinions and conclusions rests with me. No one of the above-mentioned individuals or institutions bears responsibility for any flaw in it.

Halifax, January 1994

M.H.S.

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LIST OF ABBREVIATIONS

ADB	Asian Development Bank
ASEAN	Association of Southeast Asian Nations
CGI	Consultative Group for Indonesia
CIA	Central Intelligence of America
CRS	Catholic Relief Service
CSIS	Center for Strategic and International Studies
DAC	Development Assistance Committee (of OECD)
DPR	<i>Dewan Perwakilan Rakyat</i> (House of Representatives)
EPA	Economic Planning Agency
GDP	Gross Domestic Product
GNP	Gross National Product
GOLKAR	<i>Golongan Karya</i> (Functional Group)
ICRC	International Committee of the Red Cross
IDCA	International Development Cooperation Agency
IGGI	Inter Governmental Group on Indonesia
IMF	International Monetary Fund
JICA	Japan International Cooperation Agency
JODC	Japan Overseas development Cooperation
<i>Kopkamtib</i>	<i>Komando Operasi Pemulihan Keamanan dan Ketertiban</i> (Operation Command to Restore Security and Order)
LIPI	<i>Lembaga Ilmu dan Pengetahuan Indonesia</i> (Indonesian Institute of Science and Knowledge)
LNG	Liquid Natural Gas

MFA	Ministry of Foreign Affairs
MIT	Massachusetts Institute of Technology
MITI	Ministry of International Trade and Industry
MOF	Ministry of Finance
MSA	Mutual Security Act
NGO	Non-Governmental Organization
NICs	Newly Industrializing Countries
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation Development
OECF	Overseas Economic Cooperation Fund
OTCA	Overseas Technical Cooperation Agency
OTDA	Overseas Trade and Development Association
PDI	<i>Partai Demokrasi Indonesia</i> (Indonesian Democratic Party)
PKI	<i>Partai Komunis Indonesia</i> (Indonesian Communist Party)
P.M.	Prime Minister
PPP	<i>Partai Persatuan Indonesia</i> (Indonesian United Party)
SAL	Structural Adjustment Loans/Lending
SLORC	State Law and Order Restoration Council
U.N.	United Nations
U.S.	United States
U.S. AID	United States' Agency for International Development

INTRODUCTION

A. PROBLEM SETTING

When the so-called New-Order government of Indonesia led by Soeharto took power in the mid sixties, the economy of the country was in the state of collapse. In the early sixties budget deficits had reached 50 per cent of total government expenditures, export earnings had slumped and in the period 1964 to 1966 inflation turned to hyper-inflation.¹ There were acute disequilibria. From 20 per cent of revenue in 1960, the government deficit widened up to 173 per cent in 1965, the money supply was drastically raised every year since 1960, and net reserves declined from US\$ 328 million in 1960 to minus US\$ 60 million in 1965.²

¹ For a good description of the economic condition of Indonesia before and after 1966, see Booth, Anne and Peter McCawley (eds.) (1981), The Indonesian Economy During the Soeharto Era, Kuala Lumpur: Oxford University Press, particularly chapter one, pp.1-22. See also Booth, Anne (ed.) (1992), The Oil Boom and After: Indonesian Economic Policy and Performance in the Soeharto Era, Singapore: Oxford University Press, for the latest study on economic policy-making in Soeharto administration.

² Sutton, Mary (1984), "Indonesia, 1966-1970," in Tony Killick (ed.), The IMF and Stabilization: Developing Country Experiences, New York: St. Martin's Press, tables 3.1 and 3.3, pp.69 and 71.

The national economic crisis was a legacy of the Old Order government. Political ambitions of Soekarno were believed to contribute to this situation. Two costly military campaigns caused economic deterioration. The first was a successful campaign launched in 1962 against the Dutch for Irian Jaya which became part of Indonesia in May 1963. The second was the 'policy of confrontation' with Malaysia which lasted from 1963 to 1966. It is estimated that during 1960-1965 over one-third of the foreign loans accumulated by Indonesia were exhausted for military expenditure. Another significant drain on resources during this period was the non-productive investments of political prestige projects such as national monuments and tourist hotels, which were intended to inspire national unity and were accorded priority in the government budget.

Unlike its predecessor, the New-Order government subsequently emphasized economic rather than political development. The Soeharto regime gave first priority to the rehabilitation and stabilization of the economy. The objectives were to create wider and equal opportunity for state and private, domestic and foreign interests to take part in economic development; to achieve the so-called 'balanced' budget; to pursue a rigid yet well-directed credit policy of the banking system; and to establish a proper link between the domestic and the international economy through a realistic exchange rate. From 1967 the government adopted the so-called

'balanced' budget policy. It means that the government expenditure is limited to the sum of domestic revenue and external loans. Instead of printing money, the government uses foreign loans, described as foreign 'revenue' to finance deficits. The Soeharto administration also negotiated the rescheduling of the existing debt inherited by the Soekarno regime with creditor countries. The government also sought to get foreign assistance from Western countries. In 1967 both Indonesia and Western donors agreed to establish the so-called Inter-Governmental Group on Indonesia (IGGI)³, an informal multilateral organization whose role would be to discuss Indonesia's needs of assistance, and the policies or conditionalities each donor would have in disbursing its aid.

The economic rehabilitation and stabilization program of Soeharto seemed to get the attention of Western donors. From then on the foreign aid received by Indonesia always increased and its share to the financing of development programs in Indonesia became significant. Corrective economic policies and foreign aid stimulated economic dynamism of the New-Order government in its early years. As a result, the annual growth rate from 1968 to 1973 averaged 8.7 per cent compared to the average rate of 1.7 per cent in the preceding six years.

For the last 25 years, Indonesian development has resulted in impressive outcomes such as a persisting high rate

³ Posthumus, G.A. (1972), "The Inter-Governmental Group on Indonesia," Bulletin of Indonesian Economic Studies (BIES), Vol.VIII, NO.2, July, pp.55-66.

of economic growth, the improvement of living standards and the reduction of the number of people living under the poverty line. The achievements of Indonesian development are praised by the World Bank. Some specific indicators can be mentioned here.⁴

- The number of people who live under the poverty line drastically fell from 60 per cent in 1970 to 15 per cent in 1990.
- The infant mortality rate declined from 128 per 1000 in 1965 to 68 in 1990.
- Life expectancy rose from 45 years in 1965 to 62 years in 1990.
- The population growth rate was reduced from 2.4 per cent in 1965 to 1.8 per cent in 1990.
- The literacy rate rose from 39 per cent in 1960 to 82 per cent in 1990.

Until 1981, the trends of the total amount of foreign assistance to Soeharto's Indonesia demonstrated significant increases, except in 1972 and 1976-77. In the four consecutive years, i.e. from 1982-85, the trends were decreasing, caused by the economic recession in donor countries. From then on,

⁴ The chairman of Consultative Group for Indonesia (CGI), Mr. Gautam Kaji, expressed the praise for the impressive achievement of Indonesia development in his "Opening Statement By Chairman," a speech presented the first meeting of the CGI in Paris, in July 16, 1992. See also data on "Human Development Index" (HDI) of Indonesia in United Nation Development Programme (UNDP) (1993), Human Development Report 1993, Oxford: Oxford University Press.

Indonesia has again enjoyed increasing aid, except in 1990 the aid slightly fell down. Donor countries seem to insist on giving foreign aid to Indonesia for some years to come. This tendency can be seen by the enthusiasm of the new World Bank-led donor consortium for Indonesia in responding the aid request from the government in July 1992. This consortium, called Consultative Group for Indonesia (CGI), was established immediately after IGGI chaired by Netherlands was dismissed because of political strain occurring in Dutch-Indonesian aid relations. CGI provided aid package bigger than IGGI did.

There is an interesting thing to look at in the composition of total of foreign aid disbursed annually by donor countries to Indonesia. In the early years of Soeharto's regime, the U.S. was a leading donor in providing assistance to Indonesia. Since 1974, the leading donor is no longer the U.S. It has been replaced by Japan, and now Japan is moving far ahead in giving foreign aid in terms of quantity. On the contrary, the share of the U.S. aid to the total aid Indonesia receives decreases every year.

B. RESEARCH QUESTIONS

Before formulating some questions which will be dealt with in this study, an assumption should be proposed here that the practice of foreign aid will exist and continue to exist

if both donor and recipient countries get benefit from it. On the contrary, the foreign aid practice will be terminated if either or both sides consider that the practice is no longer beneficial to any extent.

There are two important questions which I am going to address in this study: First, How does the New-Order government of Indonesia benefit from foreign aid? Second, Why do donor countries persist in providing aid to Indonesia? The analysis will take a look at the politics of aid relations between donor and recipient countries. The study will limit itself to look at major donor countries. By looking at the statistical data, we find that there is a shift in the rank or composition of donor countries providing aid to the New-Order government of Indonesia. In its early years, Soeharto's government received most of its aid from the U.S. This condition lasted until when Indonesia enjoyed its first oil boom. After that, Japan took over the U.S.'s position as the largest donor for Indonesia until now.

C. LITERATURE REVIEW

The practice of foreign aid was initially conducted by the US when it launched the so-called Marshall Plan, officially the European Recovery Program. The plan provided \$13 billion (\$60 billion in 1985 dollars) through the

organization for European Economic Cooperation (now the organization for Economic Cooperation and Development, OECD) over a period of four years.⁵ This program had two aims: Economically, the aid would be able to recover the economies of the recipients devastated by the World War II; Politically, it was hoped that it would consequently strengthen the (Western) Capitalist bloc against Communist Soviets. As the secretary of State, George C. Marshall, stated in his address at Harvard Commencement June 5, 1947, the Marshall Plan was intended "to assist in the return of normal economic health in the world, without which there can be no political stability and no assured peace."⁶ From then on, the donor country was no longer only the U.S. There now were 18 country members of OECD which provided foreign aid bilaterally. In addition, 10 OPEC countries have started giving aid to developing countries since they got petro-dollar surpluses in the early 1970s.⁷ At the multilateral level, we saw many international (financial) institutions giving aid to developing countries. Among of them were the World Bank and regional development banks for Asia, Africa, and Latin America.

⁵ Krueger, Anne O., et. al. (1989), Aid and Development, Baltimore, Maryland: The John Hopkins University Press, p.2.

⁶ Hoffman, Stanley and Charles Maier (eds.) (1984), The Marshall Plan: A Retrospective, Boulder: Westview Press, p. 100-1.

⁷ World Bank (1990), World Development Report 1990, table 9. See also OECD (1992), Geographical Distribution of Financial Flows to Developing Countries. The latter provides data on foreign aid disbursement annually.

1. EFFECTS OF FOREIGN AID

In the literature of political economy, we know there is a long debate on the effectiveness of foreign aid toward the development of the recipient countries. The early theory of foreign aid comes from the neo-classic economists: Chenery's "two-gap model".⁸ According to this theory foreign aid can substantially increase domestic saving, which is needed for the desired level of investment, in order to achieve ideal economic growth. Foreign aid also can be used to pay for imported goods and services when the recipient countries have a foreign exchange shortage. The former is called "saving-investment gap" and the latter is called "trade gap".⁹ The country cases of foreign aid success are Greece, Taiwan and South Korea.

Criticism of foreign aid practice comes both from liberal and neo-Marxist writers. Critics from the liberal perspective emphasize that aid is against the interest of economic development. Aid just strengthens the power of the ruling elite in the recipient countries and often does not touch the poor. Bauer is really vocal in this side. From the neo-Marxist writers, Hayter is the one of prominent critics; the purpose

⁸ See Chenery, Hollis B. & Alan M. Strout (1966), "Foreign Assistance and Economic Development," The American Economic Review, Vol.LVI, September, No.4, Part 1, pp.679-733.

⁹ Pomfret, Richard (1992), Diverse Paths of Economic Development, New York: Harvester Wheatsheaf, p.143.

of aid is regarded as the perpetuation and extension of international capitalism and support for the political motives of the neo-colonial power. Aid, they conclude, does not help the poor. Instead, it only hurts them.

Peter Bauer radically criticizes the existence of foreign aid practice. He rejects the practice of foreign aid,¹⁰ arguing that the development of a country is not influenced by the aid inflows. Aid does increase the resource of the recipient government and promote investment, but it does not mean that it will accelerate the rate of growth. Development requires some other factors which are conducive to economic growth, such as people economic aptitude, social institutions, political arrangements, natural resources and market opportunities. The problem of capital shortage can be solved from commercial market or private flows which are paradoxically restricted by the recipient government.¹¹ Aid can damage the development process because donor countries often induce conditionalities which might be inappropriate to the conditions of the recipient country. The argument that aid is for the economic development of the recipient countries, that aid is intended to relieve poverty, and that aid can

¹⁰ Bauer, Peter (1971), Dissent on Development, London: Weidenfeld and Nicolson, pp.95-135. Bauer (1981), Equality, the Third World and Economic Delusion, Cambridge, Massachusetts: Harvard University Press, pp.86-137. Bauer (1984), Reality and Rhetoric, Cambridge, Massachusetts: Harvard University Press, pp.38-72.

¹¹ Bauer (1971), Op Cit, p.109.

promote exports and employment in donor countries are invalid because of much evidence to the contrary. Many anomalies occur in the practice of foreign aid. Aid does not go to the poor people of the recipient countries. Instead, only a small number of people in the recipient countries will enjoy aid money. They are usually the urban elite who have power and are usually richer than some taxpayers in the donor countries who pay taxes for aid program. Foreign aid is a process "by which poor people in rich countries help rich people in poor countries."¹² Another anomaly is that it is often the case that, for the sake of relieving poverty, aid goes to a recipient country whose regime is authoritarian-militarist, undemocratic and whose politics are hostile and unfriendly toward the donors.¹³ Therefore the practice of aid should be stopped.¹⁴

Hayter, as a neo-Marxist or left wing writer, who concentrates on the study of the practice of foreign aid mostly by the World Bank and Western donors, argues that there is a political bias in disbursing aid. Aid is used as a political means for the donors to achieve their political purposes. It is not the development purposes which are considered in providing aid. Regimes which are hostile against

¹² Ibid, p.115.

¹³ Toye, John (1989), Dilemmas of Development, Oxford, UK: Basil Blackwell, pp.141-2.

¹⁴ Bauer (1984), Op Cit, pp.93-6.

the West or have left-political orientation would not receive aid. On the contrary, countries which politically go along with the Western bloc would receive aid even though their political regimes are militaristic, dictatorships, and not democratic, contrary to the political principles highly respected by the Western countries. This political consideration is also reflected in the decision making process of aid allocation in the World Bank. In rhetoric, the policy of the Bank on aid is projected to "the poorest of the poor". In reality, political and strategic considerations will decide where the money should go.¹⁵

There is no single answer on the question of the role of foreign aid toward the development of the recipient. Every study has its own country case which supports its arguments. We believe that when we study the effectiveness of foreign aid, we should treat it case by case. In its 1991 annual report¹⁶, the World Bank states that foreign aid can have both negative and positive effects on recipient countries. The report lists at least seven points of the negative effects of aid. (1) Aid can postpone improving macroeconomic management and mobilizing domestic resources. (2) Due to political reasons of the donor countries, aid can postpone fiscal

¹⁵ See Hayter, Teresa and Catharine Watson (1985), Aid: Rhetoric and Reality, London: Pluto Press Limited. See also Hayter (1971), Aid as Imperialism, Harmondsworth: Penguin Books.

¹⁶ World Bank (1991), World Development Report 1991: The Challenge of Development, Washington, D.C.: IBRD, pp.47-8.

reform. (3) When aid benefits lobbies that have a strong vested interest, it makes policy reform more difficult. (4) Aid quite often replaces domestic saving, flows of trade, and direct foreign investment. (5) When aid flows on and off, due to the political reasons of the donors, it will interrupt development programs of recipient countries. (6) Aid will not be fully effective when there is no coordination among bilateral agencies. (7) Aid will not be effective if the domestic administration of recipient countries is so weak.

Aid also has positive effects, as reported by the study. (1) Aid may improve the credibility of economic reforms. (2) It provides resources for investment and finances projects which could not be undertaken by the private sector. (3) Aid provides opportunity for personnel training. (4) When supported by good domestic policies, institutions, and administration, the aid project will be successful. (5) Aid also can support better economic and social policies.

Some studies done by Cassen and Associates¹⁷, Mosley¹⁸, and Krueger, *et.al.*¹⁹ indicate that the effectiveness of aid toward the economic development of the recipient countries, will depend on both donor and recipient. Aid will be effective

¹⁷ Cassen, Robert and Associates (1986), Does Aid Work?, Oxford, New York: Clarendon Press.

¹⁸ Mosley, Paul (1987), Overseas Aid: Its Defense and Reform, Sussex, Great Britain: Wheatsheaf Books Ltd.

¹⁹ Krueger, Anne O. (1989), Aid and Development, Baltimore, Maryland: John Hopkins University Press.

if there is the same perception on the purpose of the aid between donor and recipient countries. One thing that should not be forgotten is that the influx of aid is not the only factor which affects economic development. Its effectiveness also will be determined by the environment in which the economic development scheme or program is adopted. What is meant here by "environment" includes three major components: (1) physical, institutional, and human infrastructure, (2) macroeconomic framework, and (3) microeconomic incentive structure.²⁰ Generally, the failure of aid is caused by some factors such as the excessive intrusion of political or commercial interests of the donors, political ambitions of the recipients, mismanagement of aid, and administrative deficiencies. These studies agree in one thing, although there are some failures in foreign aid practices, it does not mean that foreign aid should be terminated. Instead aid should be defended and reformed to achieve the desired objectives.

2. MOTIVES FOR PROVIDING AID

The study of foreign aid is not merely dominated by the economic analysis on the effectiveness of aid towards the development of the recipient countries. It also deals with the political relations of both sides, donor and recipient,

²⁰ Ibid, p.28.

because the practice of foreign aid is a reflection or result of the political decision making process. When a donor country decides where its aid money should go, political considerations will always occur. The same thing with the recipient countries. Political considerations will also affect the recipient country in deciding to receive the assistance. For this study, the scope will only be limited to the donor's side.

It might be true that aid supports the recipient government to develop their economy but the achievement or the success of the development itself is not merely because of foreign aid. If the rate of economic growth of the recipient countries raises after foreign assistance inflows to the countries, we should take into account such as the domestic policies, administrative capability, and the management of the countries, as mentioned above. Griffin and Enos²¹ questioned the objectives of the aid practice. They come to a conclusion that if there were a positive effect of foreign aid toward the economic development of the recipient, it is not exactly the main objective of the donor in providing assistance. It is just a consequence instead. The main objective of donor countries in giving aid is to serve their national interests.

²¹ Griffin, K.B. & J.L. Enos (1970), "Foreign Assistance: Objectives and Consequences," Economic Development and Cultural Change, Vol.18, April, pp.313-27.

McKinley and Little²² develop two models in examining aid politics: (1) Recipient Need Model and (2) Donor Interest Model. The first model assumes that the recipient country receives foreign aid according to its economic and welfare needs. The second model assumes that the foreign policy interest of the donor country will be reflected in the distribution of aid.

For model one, the hypothesis goes as follows: The amount of assistance received by each Developing country is proportional to its economic and welfare needs. The model assumes that aid will be disbursed to a country which lacks domestic resources or foreign exchange, as proposed by "two-gap" model of neo-classic economists. Per capita aid, regarded as a dependent variable, will be determined by some independent variables such as per capita Gross Domestic Product (GDP), per capita calory consumption, numbers of doctors per hundred thousand population, size of international liquidity holdings as a percentage of imports, rate of growth of real per capita GDP, and gross domestic fixed capital formation as a percentage of GDP.

²² McKinley, R.D. & R. Little (1977), "A Foreign Policy Model of US Bilateral Aid Allocation," World Politics, Vol. XXX, No.1, October, pp.58-86. McKinley & Little (1978), "A Foreign Policy Model of the Distribution of British Bilateral Aid, 1960-1970," British Journal of Political Science, Vol. 8, Part 3, July, pp.313-31. McKinley & Little (1979), "The US Aid Relationship: A Test of the Recipient Need and Donor Interest Model," Political Studies, Vol. XXVII, No.2, June, pp.236-50.

The donor interest model has a hypothesis that the amount of foreign assistance provided to each Developing country is proportional to its level of interest to the donor. In this model, the size of the aid received, as a dependent variable, will be determined by one or all of the donor's interests such as, the maintenance of a sphere of influence, discouraging association with Communist power, power politics, economic development, and political stability and democracy.

McKinley and Little's studies based on the time-series data of foreign aid disbursed by the Western countries, especially the US and Britain from 1960-1970, come to the conclusion that the donor motives or interests, not recipient's need, are the main consideration in providing aid and determining where that money should go.

The motives of donors providing aid are so diverse. The interests of donors attached to their practices of foreign aid could take one or combination of the following objectives such as: to maintain a sphere of influence, political or military alliances, to promote their own export trade, to maintain cultural links. The aid practice of the donors might serve different motives in different places. In allocating their aid, donor countries have different motives. In one place, a donor might pursue one motive but in another place its aid is intended to serve another motive.²³ This feature of motive

²³ White, John (1974), The Politics of Foreign Aid, London: The Bodley Head, p.34.

depends on the importance of the recipient perceived by the donor. The donor might also pursue not just one motive in disbursing its aid to a Developing country.

a. Political Motives

Aid is used as a means to achieve political objectives. When we look at the origin of foreign aid practice, it is clear that "cold war consideration" is a driving force for donors to give foreign aid to Developing countries.²⁴ According to Morgenthau, development aid does not differ from the bribes traditionally employed in diplomacy especially before the nineteenth century.²⁵

Aid is used to win friends for the donor country and increase its bargaining power in the United Nations and other international fora. It is also used to help a new regime whose political orientation goes along with the donor's to consolidate its position or to support it to win an election in its domestic politics. When assistance is disbursed for a

²⁴ Maizels, Alfred & Machiko K. Nissanke (1984), "Motivations for Aid to Developing Countries," World Development, Vol.12, No.9, pp.879-900.

²⁵ Ohlin, G. (1970), "The Evolution of Aid Doctrine," in Bhagwati, Jagdish and Richard S. Eckaus (eds.), Foreign Aid: Selected Readings, Harmondsworth: Penguin Books Ltd, pp. 21-62. See also Morgenthau, Hans (1962) , "A Political Theory of Foreign Aid," The American Political Science Review, Vol. LVI, No.2, June, pp.301-9.

Developing country whose regime is unfriendly, it is used to *quid pro quo* for such as base rights and the UN votes.²⁶

b. Security Motives

Assistance is used by the donor countries for security motives. Since assistance is successful in promoting economic development of the recipient country, the economic gap can be bridged or improved and in turn, it will maintain political stability. It is believed that domestic political instability can invite outside powers to offer help.

When the security factor is considered by a donor in deciding to provide aid to one country, there are some ultimate objectives behind that security consideration. Presumably, by maintaining the political stability of the recipient country, the donor can keep the recipient away from revolutionary movement whose political orientation is against the donor's. Economically, when domestic political stability exists, the market for the donor's products, or the donor's private business interests there can be maintained.

²⁶ See Huntington, Samuel P. (1970-71), "Foreign Aid for What and for Whom (Part 1)," Foreign Policy, No.1, Winter, pp.161-89.

c. Economic Motives

Aid is also used to pursue the economic objectives of donor countries. Aid is often tied to the purchasing of goods and services from the donor providing the aid. It can be used to promote the exports of the donor country, provide jobs in domestic industries of the donor country, and promote investment.

d. Social-Cultural Motives

For some donor countries, aid also can be used to promote their cultural ties with their ex-colonial countries. This assistance is usually provided in the field of language and cultural education.

e. Humanitarian Motives

This type of assistance is accidental in manner. It helps people who get natural disasters and are victim of war. Humanitarian aid happens commonly at the level of private donation conducted by Non-Governmental Organizations (NGOs) which directly help and finance the poor and Huntington believes that it does not happen in government to government aid relations.²⁷

²⁷ Huntington, Samuel P. (1970-71), Ibid.

3. AID PRACTICE IN THE POST COLD-WAR ERA

When the Communist bloc was dismantled in early 1990, foreign aid politics was questioned. It was predicted that the practice of foreign aid will lose its justification and consequently its amount will decrease, as if it is not relevant any more.²⁸ It is so because the ideological confrontation between the Capitalism and Communism for which the aid served is absent.

At the same time, advocates of foreign aid argue that the post old War era will give the decision makers in the donor countries or international financial agencies like World Bank a chance to direct foreign aid in merely promoting development purposes. Its disbursement should be tied to good governance, sound management, democracy, good economic policies, the record of human rights violation of the recipient, environmental matters, gender issues, and the ideal of alleviation of poverty.²⁹

²⁸ See Griffin, Keith (1991), "Foreign Aid after the Cold War," Development and Change, Vol. 22, No.4, October, pp.645-85.

²⁹ For the discussion on aid policy as mentioned above, see IDS Bulletin, Vol.24, No.1, January 1993, UK: University of Sussex; Riddell, Roger C. (1992), "The Contribution of Foreign Aid to Development and the Role of the Private Sector," Development: Journal of the Society for International Development, No.1, pp.7-15; Lewis, John P. (1993), Pro-Poor Aid Conditionality, Policy Essay No.8, Washington, D.C.: Overseas Development Council.

For the years to come, the Developing countries will be in a hard position to get development assistance. The conditionality attached to the disbursement of development assistance will be more explicitly actualized. Conditionality can be defined as the result of "bargaining process"³⁰ between donor countries or international financial agencies on the one side and the recipient government on the other side, which manifests in "the set of changes in economic policy that the recipient government must implement in return for a loan or grant."³¹

In 1980, the World Bank introduced the Structural Adjustment Loans/Lending (SALs). This non-project policy-based lending is intended to support the recipient countries which are willing to conform to the structural adjustment program. Some policy measures in terms of structural adjustment which should be implemented as a conditionality for the recipient

³⁰ Mosley *et.al* (1991) define "conditionality as bargaining process" in the sense that conditionality is not the final state reached by both donor and recipient. There are three stages of conditionality game, that is, negotiation process, implementation process of the above negotiation result, and the response by donor to disburse or refuse assistance based on the recipient performance in implementation stage. See Mosley *et.al.* (1991), Aid and Power, The World bank and Policy-Based Lending, London and New York: Routledge, especially part II, pp.65-178.

³¹ Mosley (1988), "On Persuading A Leopard to Change His Spots: Optional Strategies for Donors and Recipients of Conditional Development Aid," in Bates, Robert H. (ed.), Toward A Political Economy of Development, A Rational Choice Perspective, Berkeley, C.A.: University of California Press, p.47-8.

countries to have SAL finance are covered in the headings of trade policy, resource mobilization, efficient use of resources, and institutional reforms.³² The intention of structural adjustment is to make the economies of the Developing countries less vulnerable to future shocks and more adaptable to expected external conditions. Mosley in another study argues that structural adjustment is "devoted to achieving a boost to the supply side of an economy by the removal of market imperfection."³³ In addition, Lewis asserts that "Poverty alleviation explicitly is the goal of structural adjustment."³⁴

The inclusion of human rights in the practice of foreign aid will also be apparent in the era of post Cold War. There are two approaches to link human rights with Official Development Assistance (ODA), that is, *punitive* and *promotional*.³⁵ Basically, what is meant by the punitive approach is the donor will withdraw or postpone its aid to the recipient countries which (consistently) violate human rights

³² For the detail of the measures, see Mosley *et.al* (1991), Op Cit, table 2.3., p.44.

³³ Mosley (1992), "Structural Adjustment: A General Overview, 1980-9," in Fontain, Jean-Marc (ed.), Foreign Trade Reforms and development Strategy, London and New York: Routledge, p.27.

³⁴ Lewis (1993), Op Cit, p.39.

³⁵ See Tomasevski, Katarina (1989), Development Aid and Human Rights, A Study for the Danish Center of Human Rights, New York: St. Martin's Press for a good book-length discussion on the topics.

practice. In promotional approach, the donors include the provision of human rights in their aid policy and allocate certain percentage of their assistance for the purpose of promoting human rights. Usually, this amount of aid will go directly to the Non Governmental Organizations (NGOs) whose goals are to address the needs of the ordinary people.

The demise of the Cold War also gives hope that donor countries and international financial agencies will use development assistance as a means for introducing or promoting democratic values. As Broadbent asserts,

Four decades of Cold War contributed negatively to the inherently ambivalent attitude that Western democratic states have about making human rights and democratic institution a central concern in foreign relations.³⁶

Another issue which will characterize the disbursement of development assistance is the environmental impact assessment. Actually, environmental concerns has been included in the notion of development since 1987.³⁷ Proposals for development projects will include an assessment of their environmental

³⁶ Broadbent, Edward (1992), "Foreign Policy, Development, and Democracy," in Bauzon, Kenneth E. (ed.), Development and Democratization in the Third World: Myths, Hopes, and Realities, Washington, D.C.: Taylor & Francis, p.101.

³⁷ See The World Commission on Environment and Development (1987), Our Common Future, Oxford, New York: Oxford University Press. This Commission is often called Brundtland Commission (taken after the name of Gro Harlem Brundtland, the chairman of the commission).

impact, otherwise they will automatically generate national and international opposition.

D. THESIS STATEMENT

we would like to argue that the New Order government of Indonesia has been benefitting from the aid inflows in supporting the maintenance of their power by utilizing or investing the aid money to elevate economic growth. Since its inception, Soeharto's New-Order government believed that it is politics, as experienced during Soekarno's era, which makes the Indonesian economy stagger. Since then, economic development, which is sometimes interpreted by the amount economic growth, has become a buzz-word or slogan for the New Order government. For the New Order government the success of economic development means the legitimation of their power will be secure.

Therefore, they allocate and utilize foreign aid for the improvement of the social class which is regarded as a prospective base of their political supporters. The government of Indonesia believes that external financial assistance acts as a catalyst and helps to supplement additional domestic savings needed to raise the growth rate.³⁸ Some case studies

³⁸ Haryono, Subaliono (1985), "Indonesia," in Mahran, Hassanali (ed.), External Debt Management, Washington, D.C.: IMF, pp.224-30.

on Indonesia agree that there is positive correlation between foreign assistance and the development of the recipient country. Foreign assistance positively affects the development of Indonesia because it is optimally used by the government for investment to achieve a desired level of economic growth.³⁹

We also argue that there are slightly different dominant motives between the two largest donor countries, i.e. the U.S. and Japan in providing assistance to Indonesia. For the US, foreign assistance is meant to serve their global foreign policy objective. The way they implement their policy is determined by international conditions. When international politics was in the cold war era, the U.S. defined the global political objective as restricting the spread out of communism. Therefore, the objective of foreign aid is directed towards the containment of communism. When the cold war era is over, marked by the dismantling of the communist bloc, the U.S. came out as the only political super power and regarded themselves as the world police. In accordance with existing conditions, the implementation of foreign aid policy is directed to endorse universal human rights and democratic

³⁹ See Haryanto, Agus (1991), The Effects of Budget Allocation on External Borrowing: The Case of Indonesia, Ph.D. Dissertation in Department of Economics, University of Colorado at Boulder, Ann Arbor, MI: University Microfilms International (UMI); see also Pack, Howard and Janet Rothenberg Pack (1990), "Is Foreign Aid Fungible? The Case of Indonesia," The Economic Journal, 100, March.

principles, and sustain those values which the U.S. has defined as important.

Geographically, Indonesia is considered a strategic country for the U.S. According to the "Domino theory", when a country falls prey Communism, the neighboring country will be the next victim of Communism. Fear of the truth this theory encouraged the U.S. to seriously implement containment policy. In the first years of the Cold War era, the Western bloc saw Communism in the Southeast Asian region as a serious threat. We saw that since the Korean war, some neighboring countries fell Communism, such as Vietnam, Laos and Kampuchea (Cambodia). In some countries such as the Philippines and Indonesia, the Communist party had a strong influence in their local communities. In addition, although the Communist Party of Indonesia (PKI) was officially banned, its influence was still significant.

Foreign aid for Indonesia was used to support the New-Order government, whose political orientation tends toward the Western bloc. It was hoped that foreign aid could help the Soeharto regime to promote its economic development or stabilization program. Consequently, it would enhance domestic political stability and remove the latent Communist threat which could at time be explosive.

When the Communist bloc was dismantled, marking the period of the end of the cold war, the implementation of the U.S.'s foreign aid policy towards Indonesia was slightly

different although the basic idea was still the same, that is, to serve their political interest as the world police for democracy. In disbursing their aid, the U.S. imposed democratic values and human rights to Indonesia.

Unlike the dominant motive of the US, the dominant motive of Japan in providing foreign aid to Indonesia is economically oriented. Foreign assistance has been used to maintain the supply of raw materials for its industries. The oil price crisis in 1973-74 demonstrated that Japan was heavily dependent upon the import of oil for running its industries. Besides the fact that Indonesia was considered a supplier of important raw materials. Indonesia also has other strategic position. As the fourth biggest country in terms of population, Indonesia is a potential market for the products of Japanese industries.

Geographically, Indonesia also has strategic importance for Japanese export-import activities. The Sunda and Lombok straits located in Indonesia serve as a vital line for shipping from and to Japan. Another important line is the Malacca strait which is controlled together by Indonesia, Malaysia, and Singapore. Foreign aid is used to keep Indonesia open the vital lines for Japanese industries.

E. METHODOLOGY

1. DEFINITION

In this study foreign aid is defined narrowly as the official development assistance (ODA) flows from both developed countries and international financial organizations to developing countries, in this case Indonesia. It has two main criteria. The first is that the main objective of foreign aid is to promote economic development and the welfare of the recipient countries. The second is that it is concessional in character and has a grant element of at least 25 per cent.

The grant element can be measured from three factors, i.e. interest rate, maturity (interval to final payment) and grace period (interval to first repayment of capital). Simply speaking, the grant element would be greater if the interest rate were low, and the length of time of the funds were longer. As defined by the Organization for Economic Cooperation and Development (OECD), "a loan will not convey a grant element of over 25 per cent if its maturity is less than 10 years, unless its interest rate is well below 5 per cent."⁴⁰ The term foreign aid, economic assistance or official development assistance is interchangeably used without a

⁴⁰ OECD (1992), Geographical Distribution of Financial Flows to Developing Countries: Disbursements, Commitments, Economic Indicators 1987/1990, Paris: OECD, p.327.

different meaning. The term aid here does not include military assistance. It also deals only with the assistance which is conducted officially by the government. It excludes aid disbursed by the private or volunteer agencies.

2. FOCUS OF ANALYSIS

Chapter two will focus on the effects of the foreign aid in the political economy of the New Order. In this chapter the total amount of ODA comes from all the OECD countries and international financial agencies, which consists of ODA loans net and grants.⁴¹ Whereas the focus of the chapters three and four is on the bilateral aid relations between the largest donor countries, i.e. the U.S. and Japan on the one side and the recipient, in this case Indonesia, on the other side.

The time span primarily covered by this study is restricted from 1969 to 1991. The reason for this is that the data available to date is only up to 1991. However, in the analysis, we also will look at the period before and after the main period.

The study considers that state or government as a unit of analysis. The argument is that it is a state or government which formulates a goal and implements a policy to pursue the

⁴¹ For the detail of which countries and organizations disbursing ODA to Indonesia, see Ibid.

goal. The practice of foreign aid relations is a reflection or result of the political decision making processes of both donor and recipient countries. To analyze the dominant motive of donor countries in disbursing aid to Indonesia, we will examine the importance of Indonesia for the donor countries in achieving their national interests.

We assume that the practice of foreign aid relations will exist if both donor and recipient countries get benefit from it. The total amount of aid disbursement will be changed or the practice of foreign aid relations itself might be terminated if a vital objective which both donor and recipient pursue is questioned, or if either party considers that the practice can no longer be maintained.

Secondary resources such as books, journals, magazines, and any kinds of both Indonesian government and international organization publications are used for analysis of the study. For quantitative data, we rely primarily on the annual publications of the OECD, Geographical Distribution of Financial Flows to Developing Countries and Development Co-operation.

3. STRUCTURE OF ANALYSIS

The study will be structured into five chapters. The first chapter is an introduction. Chapter two will study the

effects of aid to Indonesia. What role the foreign aid has played in development program of Soeharto's Indonesia. An analysis will be directed to the following questions: Does foreign aid properly serve or fulfill what the government of Indonesia really needs in implementing its development program? Does the aid money go merely for economic development purposes as the criteria of disbursement ideally formulated by the donor? Does the government of Indonesia utilize it effectively? Is there any political purpose set by the government behind the allocation of aid in the development process? What are the political implications of the way the government allocates the aid? And why does the government generally take measures, or treat aid especially, as the way they do? What factors associated with the maintenance of power, drives the government to have the policies it does? All of the above questions, in fact, are aimed at analyzing the effects of foreign aid towards the economic development process of Indonesia as a recipient country and merely deal with the analysis of domestic political process within the New-Order government.

Chapters III and IV will basically deal with the following questions: What motives dominantly encourage the donor countries, both the U.S. and Japan in comparison, to provide foreign aid to Indonesia? What is the importance of Indonesia for both the U.S. and Japan? It assumes that the condition of Indonesia is interpreted slightly differently by

both of these donors in formulating their foreign aid policies or disbursement toward Indonesia. The varying interpretation is basically in accordance with their own vital interests.

The third chapter will specifically scrutinize U.S.-Indonesia aid relations. It will concentrate on the period of the first year Soeharto took power until 1973-74, the first time Indonesia enjoyed an oil price hike. In that period the U.S. was the largest aid provider to Indonesia. However, it does not mean that we will exclusively study only that period. We will interpret the trends of U.S. aid disbursement to Indonesia. The first half of the chapter discusses the international situation which was still dominantly colored by a bi-polar system, that is, the U.S. and the Western bloc on the one side and the Soviet Union and its allies on the other side. It also discusses the geographic, economic, political, and strategic importance of Indonesia for the U.S. pursuing foreign policy objectives vis-a-vis Soviet Communism. The motives of the U.S. providing foreign aid to Indonesia are related to these factors. The second half of the chapter will look at the prospect of the trend of US aid disbursement in the post Cold-War era.

Chapter IV will elaborate the aid relations between Japan and Indonesia. This chapter will assess the importance of Indonesia for Japan in deciding to allocate its foreign aid. Indonesia is regarded as a supplier of raw materials for Japanese industries, especially after the oil crisis in 1973-

74. Indonesia is also considered a market for the products of Japanese industries. These economic motives are dominant in the foreign aid decision making of Japan. A conclusion will be provided in chapter V.

THE EFFECTS OF FOREIGN AID TO INDONESIA

A. INTRODUCTION

The economy of Indonesia has grown steadily at a respectable rate for the last 25 years. The economic achievement of the New Order government can be seen by comparing the Indonesian economy of 1965 and its present condition. In 1965, Gross National Product (GNP) per capita is variously estimated at \$30 to \$55. It was lower than that of China, India, Bangladesh, and Nepal. The condition was worsened by high rate inflation. Prices at domestic market generally rose more than 500 per cent although the price of rice, a commodity which has a political and strategic meaning for Indonesia, hiked by more than 900 per cent. This bleak figure will goes further when we look at the macroeconomic condition. At that year, the deficit of the state budget reached 300 per cent of total receipts.¹ Between 1960 and 1965, the economy had grown unsteadily at an annual average rate of 1.8 per cent. Whereas the annual population growth rate at the same period was 2.5 per cent. Therefore, per capita income declined over this period.

¹ Bresnan, John (1993), Managing Indonesia: The Modern Political Economy, New York: Columbia University Press, p.55.

Now the economic condition of Indonesia is much better. Income per capita is \$645², leaving behind all those nations mentioned above. The average growth rate of GNP per capita between 1965 and 1990 was 4.5 per cent, the highest in Southeast Asia and very high for low income and middle income countries. Inflation was able to be controlled, under 10 per cent per year. The economy grew at a stable rate. From 1965 to 1980, its growth rate averaged at 7.0 per cent. from 1980 to 1990, when the world economy expanded around 2.5 per cent and the other developing economies had difficulties with Structural Adjustment Programs, the Indonesian economy grew at 5.5 per cent average.

The successful achievement in economics is partly due to the contribution of aid. Foreign aid has played a crucial role, especially in the formative years of the New Order government. Some critics argue that the economic progress achieved so far by Indonesia does not reflect the real condition. Only certain people get benefits from development, and the problem of poverty is still there. Foreign aid is only benefitting certain people and therefore the practice of foreign aid should be reconsidered.

In this chapter, I would argue that the government has utilized the aid efficiently not only in terms of economy but also in that of politics. The government spends aid money in the direction of what they regard as a strategic sector. What

² Asia Week, November 3, 1993, p.53.

is meant by "strategic" sector is the economic sector which is regarded as urgent to handle immediately, otherwise domestic political stability will be disrupted and the government's power or legitimacy will be questioned. It can also be said that it is the economic sector which bears the most beneficial result to support or strengthen power. The study comes to a conclusion that aid in Indonesia contributes to the economic development. Economic development, in turn, contributes to political stability such as the New Order government now enjoys.

Before examining the aid allocation or spending policy, the model of new order government will be discussed in order to equip us with some understanding on the rationale which makes the New Order government take measures or policies the way it does. The next section will look at the history of foreign aid in Indonesia. This section will study the existence of a donor consortium for Indonesia and the total amount of ODA the New Order government has received so far. Following this section is the aid allocation or spending policy of the new order government. The question which we attempt to answer why the government spends aid money the way it does. What is the political importance of the aid spending policy with respect towards the political purpose of maintaining the status quo. The chapter will be closed with a conclusion.

B. MODEL OF THE NEW ORDER GOVERNMENT

Soeharto came to power after the failed coup launched by the Indonesian Communist Party (PKI, *Partai Komunis Indonesia*). The former government, THE Soekarno regime, left the country in a bad condition. Soekarno was preoccupied with his big political ambition of integrating all the Dutch East Indies into an independent Indonesia. He also desired Indonesia to be a world leader in eradicating neo-colonialism and neo-imperialism. He was absorbed in his political ambition without considering the resulting economic costs. Multinational corporations, especially those owned by the Dutch, were confiscated to be nationalized without compensation. The economy was never paid serious attention and an economic plan was not systematically formulated. As a consequence, the social-economic condition deteriorated.

Table 2.1 below illustrates the difficult position Soeharto's administration inherited from the former government. From 1961 until 1966, the real Gross Domestic Product (GDP) growth was always far below 5 per cent, except in 1961 when it reached at 5.1 per cent. Even in 1965, the GDP growth was zero (Column 1). Conditions were even more severe when we consider the real GDP growth per capita. From 1961 until 1966, real GDP growth per capita was always negative, except in 1961 and 1964 (Column 2). The cost of living at the same period was increasingly sky-rocketing (Column 3).

Inflation could not be managed (Column 4). In 1966 runaway inflation was peaking at more than 600 per cent.³ From the same data, we see that the total government budget was increasingly deficit during the period. In 1960, the government budget deficit totaled at 10.2 million Rupiah (Indonesian currency). It was reaching at 16.7 billion Rupiah in 1966.⁴

Learning from the past, the Soeharto regime came to the conclusion that it was political conditions which principally caused the deteriorating economic condition. From then on, all the energy was directed to the achievement of economic development. However, to run an economic development program effectively, political stability was needed. Therefore, the New Order government evolved a strategy consisting of two measures. First, The government restructured the political system in order to keep political conditions stable. Secondly, the formulation and implementation of national development was fully trusted to technocrats.⁵ The conduct of foreign policy

³ Gillis, Malcolm (1984), "Episodes in Indonesian Economic Growth," in Harberger, Arnold C. (ed.), World Economic Growth, San Francisco, CA.: Institute for Contemporary Studies Press, p. 237.

⁴ Sutton, Mary (1984), Ibid, table 3.3., p.71. The total government budget deficit from 1960-66 went as follows (in million Rupiah): 10.2 (1960), 26.3 (1961), 47.2 (1962), 167.7 (1963), 397.9 (1964), 1602.9 (1965), and 16.7 (1966). In December 1965, new Rupiah (Rp) was introduced with 1 new Rp equivalent to 1000 old. Data in 1966 was in new Rp.

⁵ What I mean by "technocrats" here is economist-bureaucrats who are believed do not have political ambition to seek power. They come from the Economics Faculty, University

Table 2.1. : GDP Growth and Cost of Living Index

Year	Real GDP Growth %	Real GDP Growth Per Capita %	Jakarta Cost of Living Index % Increase	Annual Inflation *) (%)
1960	37.7	19
1961	5.1	2.5	26.9	72
1962	2.4	-0.1	174.0	160
1963	-2.4	-4.8	118.7	128
1964	3.8	1.3	104.7	135
1965	0.0	-2.5	305.5	596
1966	2.3	-0.3	1044.7	636
1967	2.3	-0.3	171.0	111
1968	11.1	4.3	12.8	84
1969	7.1	4.9	15.9	10
1970	7.5	3.2	12.3	9
1971	5.9	6.6	4.4	4
1972	9.4	8.5	6.5	26
1973	11.3	4.9	25.8	27
1974	7.6	2.3	40.7	33

Source: Tony Killick (ed.), The IMF and Stabilization: Developing Country Experiences, New York: St. Martin's Press, table 3.1., p.69.

*)Gillis, Malcolm (1984), "Episodes in Indonesian Economic Growth," in Harberger, Arnold C. (ed.), World Economic Growth, San Francisco, CA.: Institute for Contemporary Studies Press, p.237. From 1975-1990, the annual inflation rate are: 20, 14, 12, 7, 22, 16, 7, 9.7, 11.5, 8.8, 4.3, 8.8, 8.9, 5.5, 6.0, 9.5. (Data from 1982 are taken from Wibisana, Bima, IDS (Indonesian Development Studies) Network, 1 August 1993)

of Indonesia. They are often called "Berkeley Mafia". See Ransom, David (1975), "Ford Country: Building on Elite for Indonesia," in Weissman, Steve (ed.), The Trojan Horse, A Radical Look At Foreign Aid, Palo Alto, CA.: Ramparts Press, pp. 93-116. The genesis of "Berkeley Mafia" will be discussed in chapter three.

was intended to support the implementation of the strategy. It was much more directed to economic diplomacy, and for more than two decades, Indonesian foreign policy was characterized as "low-profile".

1. POLITICAL RESTRUCTURING

The failed Communist coup of September 1965 had a great impact on the Soeharto regime. Soon after Soeharto got the letter of March 11, 1966⁶, he banned the PKI (*Partai Komunis Indonesia, Indonesian Communist Party*) and dissolved its affiliated organizations. PKI at that time was the biggest party outside of the USSR and China. It had more than three million members and most of them were farmers or rural people. Even before Soeharto got the letter, on 10 October 1965, he had created a martial-law like body called *Kopkamtib (Komando Operasi Pemulihan Keamanan dan Ketertiban, Operation Command*

⁶ In Indonesian, it is often called by its acronym "Supersemar" (*Surat Perintah Sebelas Maret*, the executive letter of March eleven). This letter was handed by the President Soekarno to give Soeharto an authority to keep the country in order and this letter was claimed to be a legal foundation of Soeharto rise to power. Recently, there is a great debate on the genesis of "Supersemar" and no one knows where the letter is now. He was confirmed as President by the People's Consultative Assembly (MPR, *Majelis Permusyawaratan Rakyat*) in March 1968.

to Restore Security and Order).⁷ This body had unlimited powers to screen and arrest both military and civilian personnel who were suspected of "pro-communist" activities. The killing of the members or advocates of PKI at that time was everywhere. It is believed that the total number of deaths was more than 500,000 people.⁸ All the leaders of PKI were sentenced to death. Thousands of alleged supporters were held in prison camps.

Soeharto since then has systematically restructured the political system to make it stable and favorable for his national development program. There is a fundamental difference between the ways Soekarno's process of nation-building and that of Soeharto's. Unlike Soekarno who heavily relied on the glorious past of javanese Majapahit⁹ kingdom and on the same feeling of suffering under Dutch colonial rule for

⁷ In September 1988, *Kopkamtib* was replaced by the Coordinating Board for Assisting in the Consolidation of National Stability, *Bakorstanas* (*Badan Koordinasi Bantuan Pemantapan Stabilitas Nasional*). Unlike its predecessor, *Bakorstanas* would have no powers of arrest and detention. Yet, in practice, the functions of both institutions do not demonstrate so much change.

⁸ Mody, Nawaz B. (1987), Indonesia Under Suharto, New York: APT Books, Inc, especially on chapter two, "The Transition," pp.31-69.

⁹ Soekarno once said that the Independent Indonesia is as the third Republic; the first is Majapahit, the second is Sriwijaya.

350 years¹⁰, Soeharto much more concentrated on restructuring politics to keep the country stable.¹¹

To secure its power, the New Order government set up GOLKAR (*Golongan Karya*, Functional Group) as a political actor in parliament. This group was controlled by military. The members of GOLKAR were all the civil servants or bureaucrats. In 1973, after the general election, nine political parties were fused into two parties. Four parties which bore the banner of islamic ideology although each had different ideals and political views became one party, PPP (*Partai Persatuan Indonesia*, Indonesian United Party), and five parties whose political ideologies ranged from the radical nationalist to Catholic became PDI (*Partai Demokrasi Indonesia*, Indonesian Democratic Party). Consequently it became apparent that the parties never became solid parties to be the opposition of the ruling party, GOLKAR. Instead, they always had problems of internal conflict. In addition, the government interfered with those parties by placing its people into the leadership positions of those parties.

¹⁰ This number comes from the first time the Dutch came to Java island; they came as traders, not colonial ruler. In fact, there are some regions outside Java which were not touched by the Dutch colonial ruler until 1800s; for instance, Aceh was conquered around 1850s.

¹¹ Utrecht give a good comparative analysis on nation-building process in Indonesia. See Utrecht, Ernst (1989), "Indonesia: Nation-Building, Ethnicity, and Regional Conflicts," in Howard, Michael C. (ed.), Ethnicity & National-Building in the Pacific, Tokyo: The United Nations University, pp.309-31.

Although the political system had been simplified, the political condition was still regarded as fragile, especially every five years before the general election time comes. It was caused by the competing ideologies of each party. The ideological differences sometimes come to the surface and political conflicts could disrupt the national development process. In 1982, the government restricted the movement of political parties by introducing the so-called "floating-mass" system. The parties were forbidden to campaign in villages. In May 30, 1984 the government enacted a law which recognizes *Pancasila* (literally means Five Principles, the ideology of the state) as a sole basis for all political parties and mass organizations. As a result of the implementation of the law, PPP whose symbol is *ka'bah* (the sacred building for moslem in Mecca) was to change its symbol to one reflecting any one of the five principles of *Pancasila*.¹²

Not only were political parties controlled by the government. Students and Press were also controlled by the government. The students' activities were limited within the

¹² The new emblem or symbol of PPP is "star". It seems that Islam as the religion of majority people is regarded as a "big enemy for Soeharto's regime", see Utrecht, Op Cit. This trend is apparent after the Iran Revolution led by Khomeini whose influence colored the life of students in big universities. The government restricted the Islamic discussion clubs which flourished in Universities. The government forbade female students and officials to wear *jilbab* (Islamic wearing). The government also took harsh measures to treat Islamic movements. For a good description on an episode of Islamic movements, see Bresnan, Op Cit, chapter "Tanjung Priok"

scope of academic activities. They were not allowed to carry on political activities inside the campus. The self-control mechanism was implemented in the Press. The government could cancel the newspaper's publishing permit if it criticized the government's policies. In short, the government had effectively institutionalized its desired political system.¹³

2. ECONOMIC DECISION MAKING PROCESS

William Liddle once asserted that Indonesia is a model that "economic liberalism is not necessary to go together with political liberalism."¹⁴ Compared with Soekarno's regime, the economy of New Order government was more open to International economic forces. This was caused by two factors: (1) the pressure of donor countries and (2) Market-oriented ideology of economic advisors. Since the New Order government relied heavily on the inflows of foreign aid, it had to accept the conditionalities imposed by the Western donors.

As mentioned above the formulation of economic policies was handed over to the group of economist-technocrats. They came from the University of Indonesia and were mostly trained

¹³ See, Liddle, R. William (85), 'Soeharto's Indonesia: Personal Rule and Political Institution,' Pacific Affairs, vol.58 no.1, Spring, pp.68-90.

¹⁴ Liddle, R. William (1987), "Indonesia in 1986: Contending with Scarcity," Asian Survey, Vol.XXVII, No.2, February, pp.206-18.

in the U.S. educational system. Actually, the relationship between Soeharto and the economist-technocrats had been forged before Soeharto became President.¹⁵ Soeharto trusted them to handle the economy of the nation because besides the fact that they were not affiliated with any political party and they did not have political ambitions, the situation at that time required expertise. They were utilized by Soeharto to gain sympathy from Western donors. Both technocrats and donors had the same perception on the strategy of economic development; Their perceptions were market-oriented.

In the history of the New Order, there was another group which sought to influence the President in taking decisions on economic matters. They were often called "engineers" or "nationalists".¹⁶ They believed in the promotion of protectionist policies to develop internal state enterprises, instead of opening the domestic market, because the enterprises were not yet able to compete in either the domestic or international markets. The protectionist barriers

¹⁵ See, Liddle, R. William (1992), "The Politics of Development Policy," World Development, Vol.20 No.6, June, pp.793-807.

¹⁶ Liddle (1986), Op Cit, p.207. They are personified by B.J. Habibie (Minister of Research and Technology and Coordinator for the so-called "strategic industries" such as IPTN aircraft industry and shipbuilding industry, PT. PAL). For in-depth analysis of the contending role of both "economist-technocrats" and "engineers" or "nationalists" (Robison calls for the latter as "economist-nationalists"), an excellent study conducted by Robison can be used. See, Robison, Richard (1988), Indonesia: The Rise of Capital, North Sydney: Allen & Unwin Pty Ltd.

would be lifted when the economy would be strengthen enough to compete in international market.

Both groups¹⁷ competed with each other to influence the President. However, all decisions would ultimately come back to the President. Ideas from both groups were accepted by Soeharto at different times, and He had his own final strategies. There was a tendency for the ideas of the economists to be accepted when the economic situation was though. There were three periods when the economists-technocrats' advice was requested. The first was in 1966 when inflation reached 600 per cent per year, economic growth was negative and Western donors' aid was immediately needed. The second was when Pertamina was in crisis in 1975. The Third was in 1983-1984 when the oil price fell down and policy reforms are needed. On the contrary, the ideas of engineers or nationalists were accepted when the economic condition was really stable and there was no difficulty on balance of payment. This condition reflects that Soeharto is a "relatively autonomous" policy maker.

¹⁷ Actually Liddle distinguishes the Indonesian decision makers on economic matters into three groups: (neo-classics) economists, engineers or nationalists, and politicians. However, for the purpose of this study, I divide them only into two groups, because as Liddle also realizes, both groups have consistently different perspectives; whereas the group called "politicians" never have their own consistent perspective. Sometimes they are supporters of the engineers and at another times they are advocates of economists. In addition, the prominent figure of this group was no longer apparent. It used to be Sudharmono, the last vice president.

For Soeharto as politician: The economists are the producers of wealth...and the nationalists are the embodiment of his dream for more rapid progress toward an industrialized, internationally powerful Indonesia¹⁸

A recent study conducted by Woo¹⁹ provides a good analysis of the model of economic decision making in Indonesia. He finds that there is a difference between the Indonesian model of decision making and that of African states. As documented by Robert Bates, "elite-oriented rent-seeking states in Africa have systematically exploited their agricultural sectors".²⁰ Almost all of the economic policies in those states have a pro-urban bias because they are intended to further the interests of the decision makers (elite technocrats) whose interests have nothing to do with agriculture. Yet this situation did not happen in Indonesia. In fact, the agricultural sector was one of the priorities which received much attention in the New Order government,

¹⁸ For a comprehensive detail, see. Liddle, R. William (1991), "The Relative Autonomy of the Third World Politician: Soeharto and Indonesian Economic Development in Comparative Perspective," International Studies Quarterly, Vol.35 No.4, December, pp.419.

¹⁹ Woo, Wing Thye (1991), "Using Economic Methodology to Assess Competing Models of Economic Policy-Making in Indonesia," ASEAN Economic Bulletin, Vol.7 No.3, March, pp. 307-21.

²⁰ Woo (1991). Ibid, p.319, as quoted from Bates, Robert (1981), Markets and States in Tropical Africa: The Political Basis of Agricultural Policies, Berkeley, CA: University of California Press.

despite the fact that groups of decision makers were apparently limited to elite bureaucrats.

From his finding, Woo develops his model called the "corporatist state" model. By corporatist state, he defines "President Soeharto as the strong chairman of the board, the army and bureaucratic elite as the senior partners, and indigenous capital, rural sector and regional interests as junior partners."²¹ He further describes the mechanism of economic policy-making process as, "the different lobbies and advisory groups propose policy initiatives, and the President adopts those which are either compatible with his innate preferences, or vital to maintaining his position as the overarching patron."²²

3. THE CONDUCT OF FOREIGN POLICY

There is a difference in style between the conduct of foreign policy of Soekarno's and that of Soeharto's.²³ Soekarno was very aggressive in practicing the foreign policy,

²¹ Woo (1991), Op Cit, p.313.

²² Ibid, p.313

²³ For a good discussion on the nature of Indonesia's foreign policy and how it had been practiced since independence until the early 1980s, see Leifer, Michael (1983), Indonesia's Foreign Policy, London: George Allen & Unwin, published for the Royal Institute of International Affairs.

whereas Soeharto was low-profile for more than two decades and much more concentrated on national development. This approach was consistent with his assertion to, "restore domestic condition first before taking part in international politics." Soeharto's generation believed that an "assertive foreign policy was really costly and they experience the bankruptcy of the economy."²⁴ This assertion is expressed in the decision of the Provisional People's Consultative Assembly (Tap MPRS) no. XIII/MPRS/1966 section 11, "...economic interest should be significantly put ahead to that of foreign policy."²⁵

Due to the immediate need for foreign aid inflows, Soeharto restored foreign relations with international organizations and Western donors which had not been good up to that time. In 1965, Indonesia withdrew from all international organizations which were believed to have been created by the imperialist powers as their political means to keep the new Independent countries under their control. The withdrawal of Indonesia from international agencies such as the UN, the IMF and the World Bank was in protest of Malaysia's admission to U.N. as a member nation.

²⁴ Wanandi, Jusuf (1988), "The Correlation Between Domestic Politics and Foreign Policy in Indonesia," in Scalapino, Robert A. *et.al.* (eds.), Asia and the Major Powers: Domestic Politics and Foreign Policy, Berkeley, CA.: Institute of East Asia Studies, University of California, p.187.

²⁵ Sabir, M (1987), Politik Bebas Aktif, Tantangan dan Kesempatan (Independent and Active Policy, Challenges and Opportunities), Jakarta: Haji Masagung, p.209. [The author's english translation.]

Right after Soeharto came to power, Indonesia reinstated its membership in international organizations. In February 1967, Indonesia was formally accepted again as a member of the IMF and the World Bank.²⁶ To give a good impression to Western donors, Indonesia's New Order also improved its performance in a number of ways. They included: to end confrontation with Malaysia, to pay adequate compensation to the owners of the nationalized properties, and to open Indonesia to private foreign investment. These changes were also caused by the conditionalities imposed by the donor countries, especially the U.S. as a requirement in order for Indonesia to get assistance.

In the mid-1980s, Indonesia was more assertive in conducting its foreign policy. This change was due to three factors: (1) There was a regeneration, especially in the military body; (2) Economic conditions were getting better; (3) The mechanism of foreign policy process was changing.²⁷ In the military body, the "45 generation", a generation which

²⁶ Sutton, Mary (1984), Op Cit, p.79. Indonesia joined the IMF for the first time in 1954 and later, the World Bank. Although the formal re-entry of Indonesia to the IMF occurred in February 1967, in 1966 the IMF had sent its mission to help Jakarta to formulate the stabilization and rehabilitation program which would be negotiated with the Western donor countries. The World Bank formally established its Resident Staff (representatives) in Jakarta in September 1968. For the history of the relations between the Bank and Indonesia in the first years, see Thompson, Graeme & Richard C. Manning (1974), "The World Bank in Indonesia," Bulletin of Indonesian Economic Studies, Vol.X no.2, July, pp.56-82.

²⁷ Wanandi (1988), Op Cit, pp.181-2.

struggled for independence in 1945, lost power and their position was taken over by the younger generation of professional army personnel. They were more pragmatic because they did not have the emotional experience of the struggle for independence. In the area of foreign affairs, the involvement of military personnel was also reduced. Career diplomats began to take greater role. The area of government which was formerly in the hands of the military would now be in the hands of civil career diplomats. The posts of ambassadorship, although for some countries were still given to the military, were now being entrusted to professional diplomats.

Another significant factor contributing to the changes was the improved economic conditions. Some achievements of the New Order which were recognized as a model example for other Developing countries were the birth control program, the achievement of self-sufficiency in staple food, and the reduction of the population ratio who lived below the poverty line.²⁸ In addition, Indonesia was also able to maintain its momentum of economic growth, and continued manage its debt problem. This achievement contributed to Indonesia's political stability. As domestic stability was maintained, Indonesia began thinking about becoming active in international fora.

The center of decision making rested with the president with the advice of the foreign minister who was responsible

²⁸ Ching, Frank (1993), "G7 Leaders Should Welcome Dialogue with Poorer Nations," Far Eastern Economic Review, 3 June, p.30

for the implementation of foreign policy. Regarding matters of security, the president would be counselled by the commander in chief of the armed forces. Conversely in the case of the foreign economic relations, the president would get advice from the economic ministers under a coordinating minister. In addition to the conventional practice of formulating foreign policy within the executive as described above, opinions from outside the executive would be also considered as inputs in formulating foreign policy. Three sources which continuously gave their opinion on the practice of foreign policy were the Commission 1 of House of Representative (DPR, *Dewan Perwakilan Rakyat*), which was in charge of foreign and defence matters; mass media which voiced public opinion, and academic institutions such as Universities, LIPI (*Lembaga Ilmu dan Pengetahuan Indonesia*, Indonesian Institution of Science and Knowledge), CSIS (Center for Strategic and International Studies) which provided the intellectual input.

C. FOREIGN AID CONDITIONS IN INDONESIA

Before examining the role of foreign aid in Indonesia, it is necessary to look at the financial conditions, left by Soekarno, because basically the New Order government claimed that the measures it took were corrective actions. The total debt of the Soekarno regime at the end of 1965 reached more

than U.S.\$ 2 billion and most of it, around three-fifths, came from the Communist countries to purchase military equipment for pursuing the political ambitions of Soekarno.²⁹

Along with the efforts to improve its relations with Western countries and international agencies, the New Order government of Indonesia also sought to find a new package of assistance from the Western countries. However, before dealing with a new aid package, Indonesia was asked to restructure its old debt of some which was due. The debt payments (including arrears) for 1966 amounted to U.S.\$530 million. It was 70 per cent of the GDP and 132 per cent of export earnings.³⁰ The only realistic option Indonesia had was to get an agreement from its creditors, both Western and Communist countries, on debt rescheduling.

The first meeting on debt rescheduling was held in Tokyo in September of 1966. All the creditors were invited but Communist countries did not come to the meeting. This meeting was continued in Paris in December 1966 and the result was that both sides, Indonesia and its Western creditors reached an agreement on debt rescheduling. The meeting appointed Dr.

²⁹ Mahajani, Usha (1970), Soviet and American Aid to Indonesia, 1949-68, Ohio University: Center for International Studies, table on p.32.

³⁰ Woo and Nasution (1989), "Indonesia Economic Policies and Their Relation to External Debt Management," in Sachs, Jeffrey D. & Susan M. Collins (eds.), Developing Country Debt and Economic Performance, Vol.3, Country Studies: Indonesia, Korea, the Philippines, Turkey, London & Chicago: The University of Chicago Press, p.114.

Herman ABS, the Head of the board of Directors of Deutsche Bank of West Germany to study the Indonesia's debt condition and its economic ability to fulfill the repayment. In 17 Octob . 1968, Indonesia proposed to the Communist creditors the same scheme of the rescheduling which would be formulated by Dr. Herman ABS. Dr. Herman's proposal was as follows: (1) The principal debt, amounting US\$ 1.7 billion per 30 June 1966, would be repaid in 30 year installment payments of which every year payment would be U.S.\$ 57 million. (2) The interest would be paid in 15 year installments starting in 1985. This formula was accepted by the creditors in Paris (they are called "the Paris club") on 24 April 1970.³¹

Since agreement on the debt problem was reached, the New Order government proposed a new package of assistance to the creditors of the Paris club. At this stage, the IMF started to get involved actively in economic policy formulation in Indonesia. The IMF played an active role in formulating the stabilization and rehabilitation program³² whose financing came from donors coordinated under the so-called Inter-Governmental Group on Indonesia (IGGI).

The IGGI was set up in February 1967 as a continuation of the meeting between Indonesia and the Paris club. This group

³¹ Sabir, M (1987), Op Cit, p.203.

³² See Sutton, Mary (1984), Op Cit. Cf. Payer, Cheryl (1974), The Debt Trap: The IMF and the Third World, New York & London: Monthly Review Press, especially chapter 1 "Introduction" and 4 on "Indonesia: A Success Story."

was not an international organization and its structure was informal. Rather it was a forum for Indonesia and its donor consortium to discuss Indonesian economic policies and the conditionalities of donors providing assistance. As described by Posthumus,

The structure of the IGGI is informal. It is not an international organization, and it does not 'pool' bilateral assistance. Through intensive discussions and debate it has tried to harmonize several aspects of bilateral assistance policies.³³

In the early years, the IGGI met several times in a year and later it was agreed that they meet twice a year, in Spring and Fall. The objectives of those meetings were to study the progress achieved so far by Indonesia in a respective year and to consider a new package of assistance requested by Indonesia for the following fiscal year (starting from 1 April-31 March). Those meetings were always held in the Netherlands.

Three fundamental principles were agreed on between Indonesia and all the donor countries under IGGI. First, aid should be able to accelerate Indonesia's economic growth. Secondly, aid should enable Indonesia to repay its previous debt. Thirdly, the aid provided should be able to strengthen

³³ Posthumus, G.A. (1972), "The Inter-Governmental Group on Indonesia," Bulletin of Indonesian Economic Studies, Vol. VIII No.2, July, p.55.

the financial position of Indonesia so that it can repay its debt in the future.³⁴

The IGGI was very generous not only in terms of the total amount of aid Indonesia would receive but also in terms of the quality of the aid itself. The total amount of bilateral official development assistance to Indonesia would increase annually (see table 2.2). The terms of aid are soft: The repayment period would be 25 years including 7 years of grace and an interest rate of 3 per cent. Also since 1969, some of the IGGI donor countries such as Australia, Switzerland, and Norway have given 100 per cent grants to Indonesia. In some years Sweden, New Zealand, Finland, U.K., Belgium, Denmark, and Canada also gave 100 per cent grants. The grant element of ODA provided by each donor country was more than 60 per cent in the last decade. The donor country which gave the least grant element of its ODA was Japan, at 66.8 per cent, while the U.S. ODA grant element was 82.3 per cent.³⁵ This concessional aid was one of the factors which explains why Indonesia did not experience a debt crisis, compared with Mexico, Brazil, and other Latin American countries which did in the 1980s.³⁶

³⁴ Sabir (1987), Op Cit, p.205.

³⁵ It is calculated from the data provided by OECD (series), Geographical Distribution of Financial Flows to Developing Countries, Paris: OECD.

³⁶ The other two are: (1) high export orientation and (2) prudent management of the maturity structure. See, Woo and Nasution (1989), Op Cit. Their study gives a good and lengthy

Table 2.2.: Total ODA to Indonesia (in Million US Dollar)

Year	Total Net ODA
1969	329.0
1970	465.0
1971	589.0
1972	503.1
1973	616.4
1974	663.2
1975	691.9
1976	668.8
1977	515.5
1978	635.3
1979	720.8
1980	949.5
1981	975.4
1982	906.3
1983	744.5
1984	672.7
1985	603.2
1986	710.8
1987	1245.9
1988	1631.8
1989	1839.3
1990	1747.0
1991	1877.3

*) Source: OECD (series, 1977-93), Geographical Distribution of Financial Flows to Developing Countries, Paris: OECD.

analysis on the Debt Management Policy of Indonesia. Cf. Haryono, Subaliono (1985), "Indonesia," in Mahran, Hassanali (ed.) External Debt Management, Washington, D.C.: IMF, pp. 224-30.

Since 1992, IGGI has been dismissed and Indonesia no longer receives the Dutch assistance. Indonesia rejected various aid packages from the Netherlands in protest over Dutch interference in Indonesia's domestic political affairs. The Indonesian government formally sent a letter of protest to the government of the Netherlands on 25 March 1992. Three requests were made to the Dutch government in the letter: (1) To terminate the disbursement of all kinds of assistance from the Netherlands to Indonesia, (2) Not to prepare the new package of aid for Indonesia, (3) Not to hold the meetings of IGGI.³⁷

Although the IGGI had been dismissed, it does not mean that Indonesia no longer request foreign aid. The dismissal of IGGI was a consequence of the termination of aid relations

³⁷ See the report on the dismissal of IGGI in the Indonesian Weekly News magazine, Tempo, 4 April 1992, pp.13-25. Actually, not only the Netherlands which canceled their aid to Indonesia after "Dili incident" of 12 November 1991 in which some fifty pro-independent East Timorese demonstrators were killed by the Indonesian armed forces. Denmark, Belgium, and Canada also joined the Netherlands to suspend their aid. The US House of Representatives also voted a US\$ 2.3 million cut in military training assistance. However, only to the Netherlands Indonesian government took counter-action to refuse receiving assistance. The factor is not only because of the small amount of the Dutch assistance received by Indonesia (1.9 per cent of total IGGI disbursement) but also because of strong emotional drives rooted from the past experience of colonialism. Cf. Van den Ham, Allert P. (1993), "Development Cooperation and Human Rights: Indonesian-Dutch Aid Controversy," Asian Survey, Vol. XXXIII No.5, May, pp.531-39. Van den Ham gives a good analysis on the political reasons for Soeharto to reject the Dutch aid. See also, MacIntyre, Andrew (1993), "Indonesia in 1992: Coming to Terms with the Outside World," Asian Survey, Vol. XXXIII, No.2, February, pp.204-10.

between the Indonesian and Dutch governments.³⁸ The IGGI position was taken over by the new donor consortium for Indonesia led by the World Bank, the Consultative Group for Indonesia (CGI). The mechanism of both organizations was exactly the same. The members of both were also the same, except for the absence of the Dutch, and that South Korea joined for the first time as a donor country. Even for the last two years, CGI has disbursed the total amount of both loans and assistance (including the grant) from US\$ 4.9 billion (in 1992) to US\$ 5.1 billion in 1993, compared with the last aid disbursed through IGGI of US\$ 4.8 billion in 1991. The only country which is still not disbursing its aid to Indonesia in a protest of human right violations is Belgium. The U.S. cut its aid from US\$ 94 million (1992) to only US\$ 40.4 million (1993). Meanwhile Canada did not provide aid before, is providing U.S.\$39 million in the year 1993.³⁹

D. AID ALLOCATION POLICY

Since its rise to power, the New Order government has undertaken the so-called "balanced budget" policy. Basically,

³⁸ The termination of aid relation between both countries also does not affect the other relations in other sectors such as diplomatic, trade, culture, social, and tourism.

³⁹ Tempo, "Acungan Jempol bagi Kebijakan Makro," (Praise for the Macro Policies), 10 July 1993, p.72.

it means that the New Order government treats foreign aid as "foreign revenue". When we look at the structure of the budget, the "revenues side" is divided into two broad categories: "Domestic Revenues" and "Development Revenues". Basically, domestic revenues come from oil and non-oil revenues; whereas development revenues are provided from both program and project aid. In the "expenditure side", there are two broad categories, that is, "Routine Expenditure" which consists of posts such as personnel salaries, subsidies, and debt service payments and "Development Expenditures" for which all foreign financing is allocated.

In the early period of Soeharto's regime until the oil boom period starting in 1973, foreign financial resources, including ODA, played a significant role. They financed 20 to 28 per cent of total government expenditure.⁴⁰ Since 1968, all foreign resources have been designated in the budget under the development expenditure category. In 1969/70 77 per cent of the development budget was financed by foreign resources.⁴¹

In the oil boom era, from 1973-1982, the share of foreign resources to development expenditure decreased, averaging

⁴⁰ Cf. Fobison, Richard (1988), "Resisting Structural Adjustment: Conflict Over Industrial Policy in Indonesia," in Cailsson, Jerker & Timothy M. Shaw (eds.), Newly Industrializing Countries and The Political Economy of South-South Relations, New York: St. Martin's Press, p.29-30.

⁴¹ Robison, Richard (1992), "Industrialization and the Economic and Political Development of Capital: The Case of Indonesia," in McVey, Ruth (ed.), Southeast Asian Capitalists, New York, Ithaca: Cornell University, p.69.

around 25 per cent. This happened because of the avalanche of oil revenues and thus reduced the role of foreign financing. Its importance again increased after the decline of the oil boom, when oil no longer provided such high export earnings. In the second half of the 1980s the share of foreign financing to development spending ranged between approximately 65 per cent to 81.5 per cent.⁴² In the last two years, the share of foreign financing to development expenditure again shows its decrease, that is, around 40 per cent in Fiscal Year (FY) 1992/93 and 36 per cent in FY 1993/94.⁴³ The summary of the share of foreign resource inflows to development spending in Indonesian budget can be seen in table 2.3. below.

Table 2.3. clearly indicates that all foreign aid goes to the development spending side of Indonesia's budget, even in the first year of the New Order some funds were intended to finance the routine expenditure side. Therefore, it can be concluded that foreign aid is utilized for productive, not consumptive, purposes which domestic saving alone cannot fulfill. Foreign aid then acts as a supplement to domestic saving. A further question is, to which sector does aid go? Which sector gets high financial priority from the New Order government? Why?

⁴² Woo & Nasution (1989), Op Cit, p.115, and table 7.1. See also, Nasution (1991), "Survey of Recent Development", Bulletin of Indonesian Economic Studies, Vol.27 No.2, August, p.19.

⁴³ Indonesia Development News Quarterly, Vol.16 No.2, Winter 1993, table p.5.

In judging which sector of the economy should be given high priority to be financed by foreign aid, a government should take into account not only economic considerations but also political ones. The government should select the most productive sector in terms its importance to the economy. It means that the economic sector in which foreign aid money is invested should promote other productive activities in the chain of economic development and as a consequence, the country will be able to repay its debt in the future years. From a political standpoint, selecting the economic sector to receive financing the social structure of the country and its political history must be considered.

In fact, the Indonesian government in dealing with aid, has clearly acknowledged in its official document that,

Having realized that the significant role foreign financing can play in the future, the government keeps on maintaining the credibility of Indonesia for donor countries and financial institutions. It can be achieved by utilizing foreign aid as efficient as possible, especially to support economic activities and the construction of productive projects so that the projects will either directly or indirectly have the capabilities to repay the debt which has been used.⁴⁴

⁴⁴ Republik Indonesia (1992), Nota Keuangan dan Rancangan Anggaran Pendapatan dan Belanja Negara Tahun Anggaran 1992/93 (*Financial Note and the Draft of National Budget FY 1992/93*), p.65.

Table 2.3.: Size of Government Budget and the Share of Foreign Financing to Development Spending, in Rp. billion and percent.

Year	Routine Expenditures (A1)	Dev'ment Expenditures (A2)	TOTAL (A1+A2 = B1+B2)	Domestic Revenues (B1)	Foreign Re'nu'es (B2)	B2 as percentage of A2
69/70	216.5	118.2	334.7	243.7	91.0	76.9
74/75	1,016.1	969.6	1,985.7	1,753.7	232.0	23.9
79/80	4,061.8	4,016.1	8,077.9	6,696.8	1,381.1	34.3
80/81	5,800.0	5,920.8	11,720.8	10,227.0	1,493.8	25.2
81/82	6,977.6	6,944.0	13,921.6	12,212.6	1,709.0	24.6
82/83	6,996.3	7,362.0	14,358.3	12,418.3	1,940.0	26.3
83/84	8,411.8	9,903.3	18,315.1	14,432.7	3,882.4	39.2
84/85	9,429.0	9,954.5	19,383.5	15,905.5	3,478.0	34.9
85/86	11,951.5	10,873.9	22,825.4	19,252.8	3,572.6	32.8
86/87	13,559.3	8,333.5	21,892.8	16,140.6	5,752.2	69.0
87/88	17,481.5	9,479.8	26,961.3	20,803.3	6,158.0	64.9
88/89	20,739.0	12,256.0	32,995.0	23,004.3	9,990.7	81.5
92/93	33,196.6	22,912.0	56,108.6	46,508.4	9,600.2	41.9
93/94	37,094.9	25,227.2	62,322.1	52,769.0	9,553.1	37.8

*) Source: Republik Indonesia (1990), Nota Keuangan (Financial Note), as taken from Haryanto, Agus (1991), The Effects of Budget Allocation on External Borrowing: The Case of Indonesia, Ph.D. dissertation, Boulder: University of Colorado, table 3.4., p.48.

**) The last two year data are taken from Indonesia Development News Quarterly, Winter 1993, Vol.16 No.2, p.5.

Note:

1. The structure of Routine Expenditures consists of such the following categories as, Personnel, Debt service, Subsidies to Regions, Food Subsidy, and Oil subsidy.
2. The structure of Development Expenditure comprises such following sectors as, Infrastructure, Agriculture and Irrigation, Regional Development, Human Resources, and Industry & Mining.
3. "Domestic Revenues" comes from Oil (Oil and LNG) and Non-Oil (which consists of tax and non-tax receipts) revenues.
4. "Foreign revenues" is all kind of foreign resources inflows.

When we examine the structure of Development Expenditure in Indonesia's budget, four sectors always given high priority by the government in its development program are: Infrastructure; Agriculture and Irrigation; Human Resources; and Regional Development. Their share is more than three-fourths of total development spending. For the New Order government, these four sectors are regarded as strategic both economically and politically. Denying to consider the importance of the development of these sectors might be a potential threat for Soeharto's political legitimacy, as realized by Glassburner, "Soeharto regime is concerned with political legitimacy; and seeks to establish it in demonstration of its ability to solve the nation's economic problems effectively and equitably."⁴⁵

Sabir⁴⁶ asserts that about 90 per cent of aid is directed at maintaining and building infrastructure in various sectors, especially sectors such as transportation and road construction, dams, irrigation, and fertilizer plant complexes. The policy of allocating aid to rehabilitating and building infrastructures is based on the bad infrastructure conditions left by the Soekarno administration. This occurred because Soekarno did not seriously pay attention to the economic sector. The priority to infrastructure financing

⁴⁵ Glassburner, Bruce (1978), "Political Economy and the Soeharto Regime," Bulletin of Indonesian Economic Studies, Vol.XIV No.3, November, p.51.

⁴⁶ Sabir (1987), Op Cit, p.205.

policy set by the Soeharto regime concurs with the International Monetary Fund (IMF) and the World Bank policy that sees providing infrastructures as the prerequisite for economic growth.

Table 2.4.: Structure of Development Expenditure
(in percent of total)

Sector	69/70	74/75	79/80	84/85	88/89
Infrastructure	23.3	21.1	19.8	23.5	30.8
Agricultr & Irrigation	19.8	31.4	12.7	17.1	14.6
Human resources	11.8	8.7	19.5	22.1	22.8
Regional development	10.0	14.1	8.4	8.0	11.6
General Public Service	9.4	5.0	11.8	9.3	7.3
Industry & Mining	4.6	7.3	10.0	8.4	4.2
Capital Participation	0	10.2	11.6	2.9	2.3
Others	0.7	2.2	6.2	8.7	6.4

*) Source: same as table 2.3. above.

From the first five-year development plan initiated in 1969 to the fifth five-year development plan, the New Order stressed development of the agricultural sector. The program of self-sufficiency in rice emerged when the rice crisis happened in 1973. At that time, Indonesia experienced its lowest rice harvest and imported rice from the international

market in which the price was high.⁴⁷ Until late 1980 Indonesia was still the largest importer of rice in the world, buying 2 million tons of rice annually. That amount constituted almost 20 per cent of the rice that was on the international market.⁴⁸ In 1984, Indonesia became self-sufficient in the rice production, producing around 26 million tons, compared with 14.6 million tons in 1973 when the crisis occurred.⁴⁹ Rice output for 1993 is estimated at 30.5 million tons.⁵⁰

Agriculture is defined as a "strategic" sector and should be given first priority because more than 60 per cent of Indonesia's people live in rural areas and depend their livelihood depends on agriculture. Historically, they have easily been infiltrated by extreme ideologies and were utilized as a foundation for radical political movements which sought to implement alternative political systems. In Independent Indonesia's history, the Communist party has twice tried to impose its ideology, that is, in 1948 and 1965, and failed. Its supporters were mostly those who lived in rural-

⁴⁷ Scherr, Sara J. (1989), "Agriculture in an Export Boom Economy: A Comparative Analysis of Policy and Performance in Indonesia, Mexico, and Nigeria," World Development, Vol. 17 No.4, April, pp.543-60.

⁴⁸ Bresnan (1993), Op Cit, p.124.

⁴⁹ Gelb, Alan & Associates (1988), Oil Windfalls: Blessings or Curse?, New York: The World Bank, table 12-5, p.216.

⁵⁰ Business Monitor International (BMI) (1993), Indonesia 1993, London: BMI Ltd, June, p.6

agricultural areas. Extreme Islamic organizations far are still regarded as a political threat. They also have a rural base for their movement and activities. Their concerns, which can gain the sympathy of the people are usually the same, that is, land reform and equitable distribution of wealth.

Another sector which gets high priority is Regional Development. This sector is intended to counteract political secessionist movements, by equalizing the distribution of development benefits. Since independence, Indonesia has never been quite free from secessionist movements. Since the New Order came to power, the government faced continuously political resistances from the provinces outside Java, especially Aceh, West Irian, and East Timor. The main factor underlying the political conflict between provinces outside Java and the central island of Java (especially Jakarta) is the wide economic gap between the central island and islands outside Java. The local people feel that their natural resources are exploited by the center.

Actually, when we examine the foreign capital movement as a whole, since 1987, there have been capital outflows from Indonesia. When foreign capital inflows are subtracted from the repayment of principal and interest debt, the net capital transfer has been negative. Data from 1987 to 1989 demonstrate that the total net capital transfer is, in billion of Rp⁵¹: -

⁵¹ Since the last devaluation of September 1986, US\$ 1 is equivalent to Rp.1.644.

238, -215, and -90 respectively.⁵² With such conditions, while the Indonesian economy adjusts structurally, the continuation of foreign resource inflows, especially concessional assistance, becomes significant. This trend can be seen from table 2.3. Further, the share of foreign financing to the total development spending from 1986/87 until 1988/89 highly increases. Increases are around 69, 65, and 81 per cent respectively, compared with 32 per cent in 1985/86. Foreign aid is needed to maintain the level of development achieved so far, otherwise the budget for development spending will be drastically reduced.

E. CONCLUSION

From the study above, it is clear that the economy of Indonesia under the New Order government has grown steadily. For 25 years, Indonesia was able to boost its per capita income from only around US\$50 to almost US\$650. This achievement is partly due to the big amount of foreign aid inflows.

Donor countries have been generous in providing aid to Indonesia not only in terms of total aid, but also in terms of concessions. All kinds of foreign aid were designed to finance

⁵² IMF (1992), International Financial Statistics Year Books 1992, Washington, D.C.: IMF, p.410-11.

development expenditures in Indonesia's budget. Aid was utilized for productive investments. Four sectors were always given high priority in development spending: Infrastructure, Agriculture and Irrigation, Human resources, and Regional Development. The New Order chose these four sectors because they are strategic not only in terms of the economy but also in terms of politics.

Economically, these four factors were strategic because are regarded as highly important in running the economy and boosting its growth. Politically, those four sectors were considered as strategic also. By promoting these sectors, the New Order government was able to counteract the secessionist or separatist movements caused by economic gap. At the same time, as the government demonstrated its capability to boost economic growth, it could gain its legitimacy of power from its people.

In conclusion, foreign aid has played a significant role in keeping the economic growth of Indonesia steady, and as a consequence of this economic growth, it can also be said that foreign aid has supported the New Order government in maintaining its political legitimacy.

THE POLITICS OF AID:
UNITED STATES - INDONESIA
RELATIONS

A. INTRODUCTION

Foreign aid programs have evolved as a form of foreign policy since the implementation of the Marshall Plan. The Marshall plan was an aid package provided by the U.S. to the economies of western European countries devastated by the Second World War. Basically, since the plan, the U.S. foreign aid has been directed toward politically strategic objectives, that is, to contain Communism, by promoting the economic welfare of recipient countries. This purpose was intensified during the subsequent four decades after the Marshall Plan as the international political constellation revealed a bi-polar system. This is not to say that the practice of foreign aid lacks humanitarian, "philanthropic" initiatives or development motives of the constituents of the donor country. In fact, the humanitarian face of aid at the state or government level has been politicized to pursue political strategic purposes.

As domestic and international political-economic conditions change, so do the practice and direction of foreign aid. Other purposes are attached to the practice of foreign aid such as export promotion, employment creation, democratic-

values institutionalization, and human rights promotion -- all can be regarded as the donor's national interests. The allocation of foreign aid has also been shifting according to changing international political conditions and the interpretation of the decision makers of the political situation. In addition, the relations between donor and recipients will also determine its practice and direction. Foreign aid will be directed to countries which are regarded by the decision makers of the donor country, as favorable and supportive of the donor country's national interests.

The New Order government of Indonesia (as explained in chapter two) came to power in a victory of the right wing coalition (in which the military was the main actor) over Communist forces mobilized by the Indonesian Communist Party (PKI). This occurred at a locus of ideological conflict, between Western allies and Communism. Geographically, Indonesia had a strategic importance for the U.S.'s global political objective of containing Communism in the region. Unlike its predecessor, the New Order government was regarded by the U.S. as able to accommodate its political strategic purposes.

It is from this perspective, that foreign aid relations between the U.S. and Indonesia should be taken viewed. In this chapter we argue that the U.S. persisted in providing assistance to Indonesia because Indonesia was regarded as having political strategic importance both in terms of its

geography and of the political attitude of the New Order government. According to the U.S. Indonesia deserved aid because it met foreign aid policies criteria, evolved by the U.S. The total amount of ODA received by Indonesia continuously decreased since the early 1980s and fell drastically in 1991. We do not pretend to deny that the introduction of democratic values and human rights promotion has been a recent and new dimension in the practice of foreign aid politics. However, this trend proves that the U.S. government is consistent in their political strategic principles of foreign aid practice. The trend towards reduction of total ODA received by Indonesia can be interpreted as a shift of direction of the U.S.'s foreign aid allocation to countries which are regarded as the "high-priority" targets for the purposes of political strategic objectives without abandoning the main objective of aid practice itself.

This chapter will be structured into five sections. After this introduction, section B will study the evolution of the U.S. foreign aid program. This section will explain the formation of foreign aid policies since the Marshall plan. The purpose of this section is to demonstrate that the principles of foreign aid practice are forged and developed within the surrounding domestic and international political economy. Section C will analyze the implementation of foreign aid principles in Indonesia by interpreting the trends of the

U.S. ODA allocations to Indonesia from OECD data. Section D will give a prediction of the U.S.'s foreign aid practice toward Indonesia in the years to come. The last section will be a conclusion.

B. EVOLUTION OF THE U.S. AID PROGRAM

Before beginning to study the evolution or development of the U.S. foreign aid program, it is necessary to put forward some assumptions. First, we should bear in mind that foreign aid can fundamentally be used as a tool for achieving the national interests of the donor country in the arena of international relations. Second, although there are really some apparent improvements in the formation of aid policies, political strategic concerns have appeared to be a dominant factor for more than four decades. Third, it would be misleading to assess the U.S. foreign aid program if we just take a look at the policies which have been formulated so far without considering how the government implements the policies under real conditions. What has always happened in the U.S. foreign aid program is that formulated policies have differed from their implementation or practice. Fourth, it is actually hard for us to differentiate one phase from another in the evolutionary process of the U.S. foreign aid program, both when we analyze it from the new policies every administration

introduces and from the span of time we deliberately make it for. Whatever method we use to make it into phases, each phase shares a common principle and it should be borne in mind that each phase does not reflect its extremely specific feature.

For the purpose of this study, we would like to divide the U.S. foreign aid program into five phases or periods. This division is made in a loose manner, following the implementation of new policies. To further our understanding, we try to examine the dominant features of the domestic and international political economic conditions which shape and influence the practice of foreign aid in each of these periods.

The five periods or phases of the U.S. foreign aid program are structured as follows: The first period of 1947 - 1961 is called the 'initial' period of aid which was inspired by the success of the Marshall plan. Second, the period of 1961 - 1973 is called 'the legalized assistance' period characterized by the enactment of the Foreign Assistance Act of 1961 and the creation of U.S. Agency for International Development (U.S. AID). The third period, from 1973-1980, is the "New Directions" period in which aid was formally directed to "the poorest of the poor". It was also in this period that human rights principles were deliberately incorporated for the first time. The fourth period, occurring in the 1980s, was a hard period for the foreign aid program. The last period, starting from the dismantling of the Communist bloc which

ended the Cold War era, was "searching" period for a new formula of foreign aid practice.

1. THE INITIAL PERIOD: 1947-61

As we have mentioned before the first practice of U.S. foreign aid was the Marshall plan. It was officially called the European Recovery Program, initiated by the Secretary of State, George C. Marshall in June 5, 1947. In 1948, the American Congress passed the Economic Cooperation Act to implement the European Recovery Program. The Act authorized a \$13 billion allocation of funds over a four-year period (1948-52), most of which was to be given as grants to the European countries to buy U.S. goods.

The basic idea of the program was to rehabilitate the war-torn economies of Europe and thereby bolster the economic and political strength of the continent. The motivations behind the program were a combination of humanitarian and political security concerns. The success of the program inspired the practice of U.S. foreign aid later. Actually, there is a debate on this. Some critics of foreign aid argue that the present practice of foreign aid is different from the Marshall plan program. The success of the plan cannot be duplicated by foreign aid. Some factors which differentiate the two are as follows: First, the political and economic

settings in which both are implemented are different. The recipients of the Marshall plan were actually economies which had conditions or prerequisites to successful development, such as political orientation, infrastructure, and human capital which were conducive for economic growth. Their economic development process was abruptly interrupted by the war. All conditions, except financial capital, required as prerequisites for economic development had been there. Therefore, when foreign aid inflowed to the region, their economies could run as expected and they did not rely on aid inflows too long. Meanwhile, the setting in which the present foreign aid program was implemented in the Third World countries was in extreme contrast to that of Europe. The Developing countries not only lacked financial capital or investment but also the infrastructure, skilled people, and an economic-minded political orientation. Therefore, some continue to depend deeply on the inflows of aid without knowing when they will be able to delink from aid dependency.¹ In short, the aid in the Marshall plan had a function to the reconstruction of post war economies while present aid practice functions towards the construction of the Developing countries.²

¹ For a detail argument of the critics on this matter, see all Bauer's writing on aid as used in the first chapter of this study.

²

The Marshall plan was expanded to the Developing countries by introducing the Point Four of President Truman (in power from 1945-53) in 20 January 1949. The first form of aid is in technical and scientific assistance. In 1953, the Point Four was transformed into the Mutual Security Agency as a consequence of the Congress passed the Mutual Security Act (MSA), a bill which deliberately links U.S. aid policies to "the threat of Communists in the emerging nations of the Third World."³ In this period, aid was intensively used to strengthen allies and build up the low-income economies so that they would be less vulnerable to Communist penetration or takeover.⁴ The security concerns of aid policies reflected the intensity of the Cold war situation. John Foster Dulles once criticized that Non-aligned (neutral) policy in the context of East-West confrontation was inherently immoral. At this period, the influx of U.S. foreign aid in Asia went to Korea, Taiwan, Thailand, the Philippines, Vietnam, and Pakistan.⁵

³ Vernon, Raymond & Debora L. Spar (1989), Beyond Globalism, Remaking Foreign Economic Policy, New York: The Free Press and London: Collier Macmillan Publishers, p. 150-1.

⁴ Selim, Hassan M., Ph.D. (1983), Development Assistance Policies and the Performance of Aid Agencies, New York: St. Martin's Press, chapter 3 on "The United States of America", pp. 39-54.

⁵ Lewis, John P. (1987), Asian Development: The Role of Development Assistance, Lanham, New York, London: University Press of America with the Asia Society, p. 24.

2. THE U.S. AID FORMATION PERIOD: 1961-73

In the Kennedy administration (1961-1963), foreign aid was intentionally to serve security objectives. He did not distinguish between development and security assistance because he believed that "development aid was security assistance."⁶ This objective can be read from the legalization of Foreign Assistance Act in 1961. According to the Act, the purpose of foreign assistance is,

to promote the foreign policy, security, and general welfare of the U.S. by assisting peoples of the World in their efforts toward economic development and, internal and external security, and for other purposes.

To implement this Act, in November 1961, President Kennedy initiated the creation of U.S. Agency for International development (U.S. AID) as "the new foreign-aid program" to facilitate those purposes.

It was recognized that to contain Communism, political stability should be maintained and it could be achieved by continuously supporting the economic development program. One interpretation of this principle is that in the same year,

⁶ Eberstadt, Nicholas (1988), Foreign Aid and American Purpose, Washington, D.C.: American Enterprise Institute for Public Policy Research, p. 33.

⁷ quoted from Black, Lloyd D. (1968), Strategy of Foreign Aid, Princeton, N.J.: Van Nostrand, p.14.

Kennedy launched the so-called Alliance for Progress. It was a program to provide long-term assistance to Latin America.

There is a shift in the U.S. ODA policy between the first and the second period, although the basic idea remains the same. In 1950s, as mentioned above, aid was directly designed to contain the Soviet Union by strengthening the allies. In 1960s, however, assistance was shifted towards the strengthening a number of countries against internal subversion. The emphasis was to support "nation-building" and win the "hearts and minds" of people in the Third World.⁸

The aggressiveness of the U.S. government to contain Communism by providing aid to the Developing countries had been used by the Developing countries' leaders as a strategy to get more aid from the U.S. As recorded by Black,

...government officials in more than a few countries where Communism has not been a problem have asserted that they should "import" 1,000 communists as a means of getting a larger share of U.S. aid.⁹

⁸ Sewell, John & John Mathieson (1982), "The United States and the Third World: Ties That Bind," in Cassen, Robert *et. al.* (eds.), Rich Country Interests and Third World Development, New York: St. Martin's Press, p. 41.

⁹ Black, Lloyd D. (1968), Op Cit, p. 19.

3. "NEW DIRECTIONS" PERIOD: 1973-80

Frustrated by the situation in Vietnam at the end of 1960s and early 1970s, when economic assistance continued to be used explicitly for political strategic purposes but without any evident results, Congress turned against any aid policy proposals. In 1971 and 1972 Nixon's foreign aid proposals were defeated in Congress. It demonstrated that the U.S. people suffered from "aid-fatigue".

To restore Congressional confidence in the foreign aid program, reforms of foreign aid policies were made. These were written into law in the Foreign Assistance Act of 1973 and the Mutual Development and Cooperation Act of 1973. The Foreign Assistance Act of 1973 recognized that economic growth did not always go along with the social advancement of the poor. Instead, the poor did not benefit from the growth. The aid policy reforms of 1973, also known as the "New Directions" legislation, formally directed foreign aid to the targeted poor. Although the bilateral assistance objectives were still dominated by political security concerns, there was increasingly pressure in this period to disburse a larger share of development assistance through multilateral organizations.

The "New Directions" of U.S. foreign aid program also went along with, if not influenced by, the evaluation of the World Bank under McNamara's presidency that there had been no

"trickle down" and that to optimize the effectiveness of foreign aid, a "Basic Human Needs" strategy should be implemented. Aid should be allocated to the "poorest of the poor" by providing them nutritious food, better education, clean water, and easily accessible health care services.

In 1976, the spirit of these "New Directions" in the foreign aid program was expressed in the enactment of a new amendment which made U.S. assistance contingent upon the provision of human rights in the recipient countries. The amendment also provided Congress the power to review the executive's aid program on a case-by-case basis.¹⁰ To realize this goal, the Carter administration (1977-1981) created the International Development Cooperation Agency (IDCA) in 1979, an institutional umbrella above AID. With the institution of IDCA, from then on AID became formally separated from the direct authority of the U.S. Department of State. It was hoped that development assistance could be removed from the political strategic concerns of state. President Carter also agreed to a continuing cutback in military and security assistance.¹¹

In policy formulation, the U.S. government undertook a drastic shift in providing assistance, a good sign of "new

¹⁰ Vernon, Raymond & Debora L. Spar (1989), Op Cit, p. 159-60.

¹¹ Eberstadt (1988), Op Cit, p. 47. See also Eberstadt, Nicholas (1990), U.S. Foreign Aid Policy - A Critique, Headline Series No. 293, Summer, New York: Foreign Policy Association.

directions" to detach the provision of aid from non-development considerations. However, this sound policy has always been hamstrung in practice, dictated by security concerns. Since the signing of the Camp David Agreement, Egypt and Israel have been the largest recipient of U.S. ODA. They have received a far higher share of U.S. aid than all other recipients of U.S. ODA.¹²

4. THE HARD PERIOD: 1980s

In this period, security concerns once again began to overshadow humanitarian and development motives. The enthusiasm that once surrounded the basic human needs approach and human rights promotion initiatives in the previous decade had waned. As mentioned above, since 1980-81 over one-third of all U.S. ODA has been spent on just two countries -- Egypt and

¹² As an illustration, in 1980-81, Egypt and Israel got respectively almost 13 and 12 percent of total U.S. ODA. Whereas India, Turkey, Bangladesh, and Indonesia which were the next main recipients of U.S. ODA in order received only 3 percent for the first two and 2 percent for the last ones of total U.S. ODA. Egypt in this respect in 1990-91 left far behind the other last four. In that year, it received 32 percent of the total U.S. ODA and Israel received 8.3 percent. The other largest recipients in order were Honduras (2.4), Nicaragua (2.2), Jamaica (2.1), and Bangladesh (1.9). Turkey, India, and Indonesia only received 1.1, 0.8, and 0.6 respectively, which ranked them as twelfth, fourteenth, and nineteenth of U.S. recipient countries. For details, see the Organization for Economic Co-operation and Development (OECD) (1992), Development Co-operation, 1992 Report, Paris: OECD, p. A-64.

Israel. During the Reagan presidency (1981-89), decisions as to which countries get how much development assistance are increasingly made on the grounds of political security rather than recipients' need. In general, Reagan's foreign policy was overwhelmed by the fear of the Soviet Union's penetration of the Developing countries.

However, unprecedented domestic and international political economic conditions arose. The period of 1980s is regarded as a hard period for the U.S. economy. This condition is not restricted to the U.S. The Western industrialized countries also suffered economic recession, a slow growth rate, and a rising rate of unemployment. At the same time, many Developing countries were trapped in mounting debts and a defaulting on their repayment. Global trade flows have also been sluggish. On the U.S. side, a heavy debt in the Developing countries meant the loss of an additional 1.1 million jobs because their trade with those countries failed to grow.¹³ Other facts which seriously concerned the U.S. government are that the U.S. has been transformed from a creditor to a major debtor country and their trade deficit (mainly against Japan) approached \$170 billion in 1986.¹⁴

¹³ Brown, Janet Welsh (ed.) (1990), In the U.S. Interest: Resources, Growth, and Security in the Developing World, Boulder, San Francisco & London: Westview Press, p. 4.

¹⁴ Sewell, John W. & Christine E. Contee (1987), "Foreign Aid and Gramm-Rudman," Foreign Affairs, Vol. 65 No. 5, Summer, p. 1017.

Because of the economic recession, the public attitude towards foreign aid, surveyed by the Chicago Council on Foreign Relations has turned and remains negative. Of seven federal government spending programs tested, foreign economic aid and foreign military aid were the least popular. The majority of the public persistently want to cut back allocation for both.¹⁵ Another finding from this poll is that of U.S. vital interests regarded by the public as urgent for the government to pursue in international relations, none dealt with the development of the Third World.¹⁶

Along with hard economic conditions, a new dimension in U.S. foreign aid practice evolved. Restraints on the foreign aid budget became apparent. The pressure to cut back foreign aid not only persistently comes from the public opinion but was also legalized through the enactment of the Balanced Budget and Emergency Deficit Control Act of 1985, sometimes called the Gramm-Rudman-(Hollings) Act.¹⁷ The consequence of the Act was that some specific aid program would be cut back on a range from 10 to 50 percent, as an effort to enforce spending ceilings. For example, total U.S. bilateral ODA in

¹⁵ Rielly, John E. (ed.) (1983), American Public Opinion and U.S. Foreign Policy 1983, Chicago, Illinois: The Chicago Council on Foreign Relations, p. 5.

¹⁶ Ibid, p. 5.

¹⁷ For a more detailed discussion on Gramm-Rudman-(Hollings) Act. see Sewell, John W. & Christine E. Contee (1987), Op Cit and Obey, David R. & Carol Lancaster (1988), "Funding Foreign Aid," Foreign Policy, Vol. 71, Summer, pp. 141-55.

the years 1980-85 almost doubled from around \$ 4.3 billion to \$ 8.2 billion before the Gramm-Rudman-(Hollings) budget-cutting began. But since 1986 the bilateral ODA has been increasingly reduced until it reached st \$ 6.8 billion in 1989.¹⁸ The latest poll on the foreign aid program demonstrates that an increasing number of the public questions the practice or effectiveness of U.S. foreign aid.¹⁹

Because of the combination of the fear of Soviet penetration in the Developing World by the Reagan administration and the hard economic conditions, another dimension of the foreign aid program was apparently accepted. Adopted the policies initiated by the World Bank's Structural Adjustment Program, the Reagan administration forced the Third World countries to turn toward the free market and to welcome foreign private investment. However, in practice, security concerns still seem to dominate the disbursement and allocation of foreign aid. For example, while aid for many programs in low-income countries was sluggish between 1981 and 1987, aid for countries which provided military-base facilities such as Greece, the Philippines, Portugal, Spain,

¹⁸ OECD (various issues), Geographical Distribution of Financial Flows to Developing Countries, Paris: OECD, p. 315.

¹⁹ See Contee, Christine E. (1987), What Americans Think: Views on Development and U.S. - Third World Relations, New York: Inter Action & Washington, D.C.: Overseas Development Council.

and Turkey rose by nearly 60 percent during the same period, exceeding \$ 1.5 billion in 1987.²⁰

5. "SEARCHING" PERIOD: AFTER 1990

The dismantling of Communist bloc in Eastern Europe since mid-1989, followed by the breaking apart of Soviet Union into some independent Republics, has influenced the policies and practice of U.S. foreign aid. The spirit of containing Soviet penetration of the Developing countries as a rationale behind assistance allocation has lost its solid ground. New dimensions of foreign aid program have been initiated and are still being evolved. Ideal motives and factors of foreign aid program such as humanitarian, development purposes, environment-related matters, introducing democratic values, and human rights promotion which were always interrupted and hamstrung by security concerns, again came to the fore and for the first time were placed in a strong position.

Another factor which increasingly determines the policies of U.S. foreign aid program is the state of domestic economic conditions reflected in a growing deficit, high unemployment rates, and continuing recession. On the other side, some Developing countries which benefitted from the post second

²⁰ Obey, David R. & Carol Lancaster (1988), Op Cit, p. 152.

World War influx of U.S. aid, have "graduated" into the category of Newly Industrializing Countries (NICs), no longer in need of assistance. As a consequence, economic or trade concerns will be increasingly determinant of aid allocation.²¹

Conditionalities for U.S. foreign aid will be harder for some Developing countries.²² Not only political conditionalities, such as the introduction of democratic values and the promotion of human rights, but also economic conditionalities, such as economically and environmentally sound government management practices will be imposed by the U.S. on recipient countries through the Structural Adjustment Program advocated by the World Bank. The Task Force on Foreign Assistance has recommended to change old Foreign Assistance Act of 1961 with a new International Economic Cooperation Act

²¹ Cf. Morss, Elliott R. & Victoria A. Morss (1986), The Future of Western Development Assistance, Boulder & London: Westview Press. They give a new insight in the discussion on ODA by looking at the emergence of NICs and the steady-growth Developing economies. One of their hypotheses (pp.101-8) on the future possibilities of international cooperation is that *technical exchange programs* are to replace technical assistance activities.

²² One proposal of U.S. aid policies for the 21st century drafted by the U.S. AID demonstrates that the disbursement of assistance should be directly tied to overcoming the economic problems faced by U.S. economy. In this position, aid should be coordinated with other economic activities such as trade, investment, and debt problem. See U.S. Agency for International Development (1989), Development and the National Interest: U.S. Economic Assistance into the 21st Century, A Report by the Administrator, 17 February, Washington, D.C.: AID. This study is customarily referred to as the Woods Report, after the then AID Administrator, Alan Woods.

of 1989 which would specify four major foreign economic policy objectives, namely:

1. *Growth* = Encouragement of broad based economic-growth.
2. *Environmental sustainability* = Improved environmental, natural resources, and agricultural management.
3. *Poverty alleviation* = Human Resources Development aimed at improving the well-being of the poor and their capacity to become productive citizens.
4. *Pluralism* = Promotion of political, social and economic pluralism.²³

C. THE U.S. FOREIGN AID PRACTICES TO INDONESIA

1. FEATURES OF U.S. AID

In the first years of Soeharto's coming to power, the U.S. was the largest donor for Indonesia. The U.S. ODA inflows reached its peak in 1971 and decreased in 1972. This pattern of decrease feature went along with the trend of total ODA disbursed by the U.S. (See table 3.1., column 2 and 3, below) and since 1974, its position as the largest ODA provider has been taken over by Japan (See column 3 and 5 of the same table). In general, in the 1970s, U.S. ODA inflows to

²³ U.S. Congress. House. Committee on Foreign Affairs (1989). Report of the Task Force on Foreign Assistance to the Committee on Foreign Affairs, February, Washington, D.C.: U.S. Government Printing Office (GPO), pp. 29-30.

Indonesia was subject to considerable fluctuation, reflecting U.S. political security interests at stake in Indonesia, which will be further explained below.

From 1980 onward, it can generally be said that the inflows of U.S. ODA to Indonesia has been continuously reduced and substantially so as of the mid-1980s. This reduction, to some extent, can be seen as a reflection of the budget deficit cutting efforts of the Gramm-Rudman-(Hollings) Act in effect as of 1986. The U.S. position as foreign assistance provider to Indonesia has been surpassed by other Development Assistance Committee (DAC) countries of the Organization of Economic Cooperation and Development (OECD), such as West Germany, the Netherlands, Australia, Canada, and France.

In concessionary terms, the grant element of U.S. ODA to Indonesia in last ten years roughly averaged at 82.3 percent. This is well below the average grant element in the total ODA disbursed by the U.S. over the same period. Total U.S. ODA in this period had a grant element of 95.5 percent.²⁴ In this context, assistance for Indonesia was a little bit less concessional than aid disbursed by the U.S. to other countries. As mentioned in the previous chapter, compared with ODA from other DAC countries, U.S. aid has the second least grant element after that of Japan.

²⁴ This average percentage comes from the calculation of existing data provided by OECD (series), Geographical Distribution of Financial Flows to Developing Countries, Paris: OECD. They have provided such data as of the ODA disbursement in 1983.

Table 3.1.: Bilateral ODA (to Indonesia) from the U.S. and
Japan (in million US dollar)

Year	Total U.S. Bilateral ODA	U.S.ODA to Indonesia	Total Japan Bilateral ODA	Japan ODA to Indonesia
1969	2,754	151.0	339.7	65.8
1970	2,646	186.0	371.5	125.8
1971	2,866	227.0	432.0	111.9
1972	2,714	158.0	447.8	103.2
1973	2,341	158.0	765.2	142.9
1974	2,542	82.0	880.4	221.1
1975	2,927	91.0	850.4	197.9
1976	2,838	127.0	753.0	200.5
1977	2,897	102.0	899.2	148.4
1978	3,474	142.0	1,531.0	227.6
1979	4,076	181.0	1,968.8	226.9
1980	4,366	117.0	2,010.1	350.0
1981	4,317	103.0	2,260.4	299.8
1982	4,861	72.0	2,367.3	294.6
1983	5,563	80.0	2,425.2	235.5
1984	6,457	61.0	2,427.4	167.7
1985	8,182	43.0	2,556.9	161.3
1986	7,602	46.0	3,846.3	160.1
1987	7,007	36.0	5,134.8	707.3
1988	6,765	22.0	6,421.9	984.9
1989	6,826	31.0	6,778.5	1,145.3
1990	8,367	31.0	6,788.5	867.8
1991	9,387	18.0	8,860.3	1,065.5

Source: OECD (series), Geographical Distribution of Financial Flows to Developing Countries, pp. 153 & 315.

2. U.S. INTERESTS IN SOUTHEAST ASIA

The presence of the U.S. in Southeast Asia, at least until the end of the Cold War period, has been generally driven by political security interests despite the growth of other interests such as trade, investment, and access to raw materials. A study conducted by a Committee on Foreign Relations asserted that three major objectives shaping the U.S. policy toward Southeast Asia were as follows.

We firmly support the progress and stability of our ASEAN friends and allies as the heart of our policy toward Southeast Asia.

In cooperation with ASEAN, we seek to restrain the aggressive ambitions of Vietnam.

We seek to curb the growing Soviet military presence and influence in the region.²⁵

On the basis of our review of the trend of the U.S. foreign assistance inflows to the region, it can be argued that political security interests have always been a dominant force for the U.S. involvement in the region. Foreign aid is allegedly and apparently used as a significant tool of the

²⁵ U.S. Congress. House. Committee on Foreign Relations (1982), United States Relations with ASEAN (Thailand, Indonesia, Malaysia, Singapore, and the Philippines), Hong Kong, and Laos, Washington, D.C.: GPO, p.58. Along with the recognized objectives, Krause argues that the countries in the region "are of great political and strategic importance in themselves because they straddle crucial sea-lanes and are neighbors of troubled Indochina." See Krause, Lawrence B. (1982), U.S. Economic Policy toward the Association of Southeast Asian Nations: Meeting the Japanese Challenge, Washington, D.C.: The Brookings Institutions, p.68.

U.S. intervention in the Third World. Although the U.S. assistance program is commonly accused of having failed in promoting economic growth, they have strengthened the defense of some nations.²⁶

The Southeast Asian region to which Indonesia belongs has been regarded by the U.S. as a strategic region in the context of the U.S. global foreign policy of containing Soviet or Communism.²⁷ In his reflective thought on the Containment policy which he initiated, Kennan asserts that what is the immediate factor the policy addresses is not the threat of Soviet military aggression but its political ideology which gives an alternative for many of the then newly independent countries colonialized for many years by Western countries. As his interview reads,

The objective is not to contain the threat of Russian military because the condition of her so devastated. No nuclear weapon, 25 million of its people died and physical destruction need to be reconstructed. What Kennan thinks was the potentiality of ideological and political threat. The communist party in the world is so

²⁶ Bandow, Doug (1992), "Economic and Military Aid," in Schraeder, Peter J. (ed.), Intervention into the 1990s: U.S. Foreign Policy in the Third World, Second Edition, Boulder & London: Lynne Rienner Publishers, p. 92.

²⁷ The source of Soviet containment policy firstly allegedly comes from the article titled "The Sources of Soviet Conduct," written by George F. Kennan under the pseudonym "X" in Foreign Affairs, July 1947. It is reprinted in Foreign Affairs, Vol. 65 No. 4, Spring 1987, pp. 852-68.

unified discipline movement under the control of the Stalin regime in Moscow.²⁸

The first chosen instrument of containment was economic assistance provided for Western Europe countries through the Marshall Plan. But as the theater of intense ideological conflict moved from Europe to the Asian continent characterized by the eruption of the Korean War in early 1950s, U.S. foreign aid shifted towards Asia. This was the case until the end of 1970s, at which point the largest share of U.S. foreign assistance has gone to the Middle East, especially and exclusively to Egypt and Israel, as a consequence of the application of Camp David agreement.

Southeast Asia has been important to the U.S. because it is one of the areas where the Soviet Union attempted to break out of Western containment. The enthusiasm of containment in the region is echoed by the "domino theory" first evolved in the National Security Council in January 1954 and accepted by President Dwight D. Eisenhower as a policy guideline in dealing with the region. The domino theory predicted that the falling down of any single country in Southeast Asia into Communist control would lead to the neighboring country in the region becoming the next victim. The theory assumed that "if some key nation or geographical region falls into communist

²⁸ Deibel, Terry L. & John Lewis Gaddis (eds.) (1987), Containing the Soviet Union: A Critique of U.S. Policy, Washington, D.C.: Pergamon-Brassey's International Defense Publishers), p.16.

control, a string of other nations will subsequently topple 'like a row of dominoes' ".²⁹ This threat, and the validity of this domino theory became evident with the consolidation by Vietnam of its control over all of Indochina in the mid 1970s.

As the political security motive drives the U.S. to deal with the region generally, its important significance can also be seen with respect to aid relations between the U.S. and Indonesia.

3. INTERPRETATION OF U.S. AID INFLOWS TO INDONESIA

The emergence of Soeharto's New Order government can be seen as the victory of the military in Indonesian politics against the Communist party. In his last years, Soekarno tried to keep his power by mobilizing popular support from the PKI as a balance to the increasingly strong position of the military. The political power constellation of Indonesia at that time was pictured as a struggle of "three" political actors, in which Soekarno as a balancer and at the same time as a manipulator of the conflicting two (PKI and military). That military came out as a winner could not be completely separated from U.S. support. The main motive driving the U.S. to prop up Soeharto was due to the Soekarno's supportive

²⁹ Esterline, John H. & Mae H. Esterline (1990), "How the Dominoes Fell": Southeast Asia in Perspective, Lanham, Maryland: University Press of America, p. 4.

political attitude towards Communist bloc and hostility against the West.

Actually, the U.S. had been involved in Indonesian politics since the mid-1950s in efforts to topple down the Soekarno regime.³⁰ At that time, the Central Intelligence of America (CIA) backed up the secessionist revolutionary movement in Padang (West Sumatra) by supplying them military equipment and its military pilot with a base camp in the Philippines. The Padang rebellion was one of the center-periphery (regional) conflicts the Indonesian government has had to contend with, and it will potentially occur in the future. In that involvement, one American military aircraft was shot down by the Indonesian government and its pilot was caught.³¹

However, there are some factors that have made the position of Indonesia so important to the U.S. that it has assiduously kept up friendly relations, and a hospitable political orientation towards the government of Indonesia, even without treating it as her ally. First, geographically, Indonesia lies across the sea lines of communication between the Pacific and Indian Oceans. A hostile Indonesia could deny passage

³⁰ Tilman, Robert O. (1987), Southeast Asia and the Enemy Beyond: ASEAN Perceptions of External Threats, Boulder & London: Westview Press, pp.129-31.

³¹ For the involvement of CIA in Padang revolt, see Worthy, William (1966), The Silent Slaughter, New York: Youth Against War and Fascism, as cited by Selden, Mark (ed.) (1974), Remaking Asia: Essays on the American Uses of Power, New York: Pantheon Books, especially pp.21-49.

through the waters controlled by its archipelago and thus immensely complicate the logistics of American power projection into the Persian Gulf area. This strategic position often recalls a dilemma for decision makers in the U.S. in dealing with Indonesia. The Indonesian authoritarian regime is often accused of having abused democracy and human rights, but strategically it could contain Communism. A dilemma faced by the U.S. is whether to help them or to punish them.³²

Second, Indonesia has abundant natural resources, especially oil. This strategic natural resource has tended to dictate the formulation of U.S. policy towards Indonesia. As Richard M. Nixon (1969-74) put it: "Indonesia, which has big population and natural resources, constitutes the greatest prize in the Southeast Asian area."³³ The factor of accessible oil in Indonesia again appears to be the second priority (after Western Europe) in a general strategic planning elaborated by Pentagon officials for the Defense Secretary in May 1982. in case of world war with the Soviet Union.³⁴ The

³² See Pauker, Guy (1991), "Indonesia under Suharto: The Benefits of Aloofness," in Pipes, Daniel & Adam Garfinkle (eds.), Friendly Tyrants, An American Dilemma, New York: St. Martin's Press, pp. 379-99.

³³ Ping, Ho Kwon (1982), "ASEAN: The Five Countries," in Broinowski, Alison (ed.), Understanding ASEAN, New York: St. Martin's Press, p. 229.

³⁴ Wionczek, Miguel S. (1991), "Energy and International Security in the 1980s: Realities or Misperceptions?" in Ahoja-Patel, Krishna, *et. el.* (eds.), World Economy in Transition: Essays Presented to Surendra Patel, New Delhi: Ashish Publishers, p. 76.

U.S. oil companies operating in Indonesia participated in the U.S. government's attempt to topple the Soekarno regime.³⁵

Having recognized those factors, the U.S. has had a two-fold interest in Indonesia. Maintenance of stability in Indonesia is necessary because of its strategic position and rich mineral wealth. But another major reason has been U.S. efforts to establish a bulwark against Communism.³⁶

As Soeharto came to power, there was a promising shift of Indonesia's political stance towards pro-Western orientation. Immediately after Soeharto came to power, he banned the PKI and the slaughter of PKI members soon spread across the Indonesian islands, with the killing mostly happening in Central and East Java. The U.S. direct involvement in the PKI massacre is apparent. The U.S. embassy in Jakarta provided the army a list of PKI members which "targeted" to be killed. The CIA was deeply involved in the bloodbath by training the army and manipulating and dramatizing the news of the death of top-ranked generals killed by the PKI members so as to fire the popular hatred against the Communists. A research study

³⁵ Mody, Nawaz B. (1987), Indonesia Under Suharto, New York: APT Books, Inc., p. 51. The lobby of oil companies was so influential in forcing the U.S. to threaten to take a firm measure against Soekarno's regime if they nationalized all Western-owned oil companies. Soekarno, in fact, did not nationalize the companies. See, Payer, Cheryl (1974), The Debt Trap: The IMF and the Third World, New York & London: Monthly Review Press, pp.75-90.

³⁶ Ibid, p.51.

conducted by the CIA acknowledges the U.S. backed PKI massacre as "one of the worst mass murders of the twentieth century."³⁷

In the first years Soeharto came to power, the U.S. provided ample foreign assistance. The amount continuously increased until 1971 when Indonesia received the third largest share of total U.S.' disbursed ODA, after India and Vietnam. For the Soeharto regime, U.S. was at that time his largest donor. This significant amount represented what could be said to be a "reward" for the Soeharto regime for its pro-Western political orientation. The New Order government's Western oriented policy was supported if not directed by the appointment of the American-trained bureaucrats who hold key positions in formulating Indonesian economic development planning. Three of five Economic ministers graduated from Berkeley University. They are Wijoyo Nitisastro, Emil Salim, and Ali Wardhana. They are collectively often called as "Berkeley Mafia". Their policy is still influential until recently and one of them, Wijoyo Nitisastro, is still in the position of the advisor to President on Economic Affairs.

The "Berkeley Mafia" is the example of the importance of education as an arm of statecraft to contain Communism. The intellectuals and bureaucrats which will potentially hold the key position in the decision making process are "worked out" in order to have an expected intellectual and political

³⁷ Scott, Peter Dale (1985), "The United States and the Overthrow of Sukarno, 1965-1967," Pacific Affairs, Vol. 58 No. 2, Summer, p. 240.

orientation. They are given a scholarship to be trained within the American (Western) accepted values circumstances.

This containment method as the complement of providing foreign assistance has been systematically conducted by the U.S. since 1950s. As acknowledged by Dean Rusk, Assistant Secretary of State for Far Eastern Affairs, in 1952,

"to contain Communist aggression, not just to train American to combat it in Pacific but also to open training facilities for increasing numbers of our friends from across the Pacific."³⁸

To implement this policy Ford Foundation working together with Rockefeller Foundation provided scholarship granted to Indonesian intellectuals to study at Massachusetts Institute of Technology (MIT), Cornell, Berkeley, and Harvard. As a result, in the first "Development Cabinet" of Soeharto's, of seven influential positions for formulating economic development program, only one was held by the alumnus outside the U.S.' universities. The rest are in the hands of the graduated from Berkeley (four), Harvard (one), and MIT (one).³⁹

³⁸ Ransom, David (1975), "Ford Country: Building on Elite for Indonesia," in Weissman, Steve (ed.), The Trojan Horse, A Radical Look at Foreign Aid, Palo Alto, California: Ramparts Press, p. 95.

³⁹ Ransom, David (1975), Ibid, p.110. For the importance of the education and training program in the U.S. foreign aid program, see also Naya, Seiji (1988), The Role of U.S. Economic Aid in Promoting Development, Implications for Trade, Investment, and Human Resource Development, Honolulu, Hawaii:

In 1972 the amount of the U.S. ODA inflows decreased around 35 percent of the previous year's and remained at the same rate in the following year, that is, \$158 million before falling again in 1974, to almost 50 percent down from this figure. This declining trend can be explained from both sides with the consideration that the aid inflow cut did not bother the political security concerns of the U.S. in Indonesia and generally in the region. First, as explained in section B.3. above, the American tax-payers suffered from "aid fatigue" as a result of squandering money for political purposes in Vietnam. Second, at that time Indonesia was inundated by oil money as a consequence of quadrupling oil price hike. It was assumed that oil money would compensate the falling of aid inflows without leaving any significant political stability problem.

In 1975, the Portuguese authorities gave up maintaining its power control over the colony of East Timor. This led to the political stability caused by the fighting among the various political factions there. In 5 November 1975, the anti-Indonesian dominant leftist group called Fretilin came to power and claimed East Timor to be an independent country. For Indonesia, Fretilin's coming to power was regarded as a serious threat for its national security. This concern was also shared by the U.S. Since August 1975, Henry Kissinger

Resource System Institute, East-West Center.

(then U.S. State Secretary) had signalled Jakarta that the U.S. would agree to the Indonesians' invasion of East Timor.

On December 5, 1975, while the U.S. President Gerald R. Ford (1974-77) accompanied by Kissinger was visiting President Soeharto, the Indonesian government gave a briefing foreign ambassadors on the East Timor situation which was increasingly aggravating for Indonesia's national security.⁴⁰ Two days later, on 7 December 1975 or one day after Ford and Kissinger left Jakarta, the Indonesian sea and air forces invaded East Timor and seized the Capital. It is clear that the Indonesian invasion of East Timor was fully supported by the U.S. which sought to contain Communism and which had just witnessed the falling down of Indochina region into Communism. Kissinger is once noted to argue that "we can't construe a Communist government in the middle of Indonesia."⁴¹ He was quite certain that "No one has complained that it was aggression. Indonesia did a self-defense."⁴²

It is estimated that 60,000 people were killed during the clash and 100,000 people or 15 percent of the population died mostly of disease and starvation.⁴³ On 17 July 1976, East Timor became 27st province of Indonesia. The U.S. accepted the

⁴⁰ Esterline & Esterline (1990), Op Cit, p.316.

⁴¹ Hertsgaard, Mark (1990), "Arms and the Man," New Statesman & Society, Vol. 3 No. 125, 2 November, pp.17-9.

⁴² Ibid.

⁴³ Esterline & Esterline (1990), Op Cit, p.316.

incorporation of East Timor into Indonesia in the same year and this position has not changed under Carter administration (1977-81) which is allegedly strong in campaigning the promotion and protection of human rights.⁴⁴

In this period, the trend of U.S. ODA inflows demonstrated a relatively continuing increase, except in 1977 which showed a slight decrease. This figure becomes more interesting when we compare it to the total U.S. bilateral ODA. In 1976, while there was a decrease in total U.S. bilateral ODA, from \$2.9 billion to 2.8 billion, in the figure of U.S. ODA disbursed for Indonesia there was a significant increase, from \$91 million to \$127 million. This trend shows that the political security motive of Communist containment was still a dominant factor in determining aid allocation or disbursement.

In addition, the U.S. also had pledged \$5.5 million assistance over a period of 3 years for East Timor development, besides contributing \$2.3 million in funds channelled through the International Committee of the Red Cross (ICRC) program and \$11.04 million in funds and commodities through the Catholic Relief Service (CRS) efforts.⁴⁵ The rationale for providing these funds, without denying the humanitarian motives, goes along within the

⁴⁴ U.S. Congress. House. Committee on Foreign Relations (1982), Op Cit, p.53.

⁴⁵ Ibid.

context of containment policy. The worse the economic conditions, the more susceptible the region to Communist infiltration or penetration. Therefore, to contain Communist influence and preventing it from blooming or flourishing it was necessary to restore and promote socio-economic conditions.

In 1980s, the figure of aid inflows from the U.S. demonstrated a constant tendency to decrease. Some factors can be mentioned to explain this decline. First, the economy of the U.S. increasingly suffered from a deficit. Second, since the Camp David Accord was in effect, the Middle East, including the Gulf Area, was regarded as the intense antagonistic theater which was given high priority. As the security priority moved from Asia to the Middle East, so did the aid transfer from the U.S.

D. U.S. AID INFLOWS IN THE FUTURE

In the years to come, the aid inflows from the U.S. will be sluggish. It is so because of not only the economic problems hardly hit the U.S. such as burdensome deficit in her balance of payment and high rate of unemployment but also the end of the long lasting cold war era which makes the political security justification of providing aid lose ground. Although it almost does not make any difference, the total amount of

U.S. ODA disbursed both for (bilateral) Developing countries and multilateral institutions in 1991 showed tendency to decrease, from \$11,394 to \$11,362 million. It means that in 1990, the total amount of ODA was .21 percent of Gross National Product (GNP) while in 1991 it decreased to only .20 percent, a figure which is quite far from the expected target.⁴⁶

In addition, Its disbursement will be strictly tied. Its conditionalities will be harsh. The time of the avalanche and easiness of foreign aid is over with the ending of the era of cold war. Foreign aid will be more directed to the country whose economic performance demonstrates reasonable prospects. It will go to the countries which are willing to take the recipe of Structural Adjustment Program. Political conditionalities, such as the protection of human rights and the introduction of democratic values which were often denied in the Cold war era will be seriously tied to the disbursement of aid.

In the Cold war era, we did not see the application of human rights as one of the conditionalities for aid disbursement. The human rights principles were marginally used

⁴⁶ Having studied from the "Pearson report", the United Nation (U.N.) set up the first "Development decade" in the late 1960s for which the Developed industrialized countries were urged to transfer their money to the Developing countries at one percent of their own GNP (0.7 percent of GNP for ODA). The figure of U.S. ODA comes from OECD (various years), Development Co-operation.

as a conditionality for aid disbursement.⁴⁷ The Ford administration kept providing aid to Indonesia although they received criticism within both Congress and House to reduce or stop it because of human rights violations of ex-PKI member detainee.⁴⁸ The Carter administration, which allegedly intended to promote and protect human rights practices, supported Indonesian action in East Timor and gave additional foreign aid to Indonesia.⁴⁹

With the ending of Cold war era, everything has changed. U.S. ODA decreased almost 50 percent in 1991, from \$31 to \$18 million. In 1992, the Congress passed a foreign aid bill which froze \$2.3 million in defence training aid to Indonesia in protest of the "Dili incidence" in which 50 separatist demonstrators were killed by the Indonesian military in November 1991.⁵⁰ Actually the U.S. measure followed the cancellation or suspension of aid from the Netherlands, Denmark, and Canada. The Clinton administration has adopted a tougher stance on rights violations. In late April, the U.S.

⁴⁷ Forsythe, David P. (1989), "U.S. Economic Assistance and Human Rights: Why the Emperor Has (Almost) No Clothes," in Forsythe (ed.), Human Rights and Development, International Views, London: The Macmillan Press, Ltd., p.174-9.

⁴⁸ Newsom, David D. (1986), "Release in Indonesia," in Newsom (ed.), The Diplomacy of Human Rights, Lanham, MD.: University Press of America and Georgetown University, Washington, D.C.: The Institute for the Study of Diplomacy, pp.101-9.

⁴⁹ U.S. Congress. House. Committee on Foreign Relations (1982), Op Cit, p.52-4.

⁵⁰ Far Eastern Economic Review, October 22, 1992, p.14.

supported a resolution of the U.N. Human Rights Commission expressing "deep concerns" over violations in East Timor. Under the Reagan and Bush administrations, the U.S. helped to block similar resolutions. When the Consultative Group for Indonesia (CGI) agree to provide more aid (and loans) to Indonesia, the U.S. still criticizes the practice of human rights in Indonesia and its share in CGI decreases.⁵¹

In the years to come U.S. ODA inflows to Indonesia will be more sluggish. Political factors such as introduction of democratic values and promotion of human rights as explained above will still play an important role in the disbursement of ODA from the U.S. Another factor which will determine the trend of U.S. ODA inflows to Indonesia is the economic performance of Indonesia itself. As the Indonesian economic grows steadily, the foreign assistance inflows from the U.S. will be increasingly reduced or at least kept at the same level as the previous year. Only if there is a drastic political change in Indonesia which will disturb domestic stability, will U.S. ODA inflows increase.

E. CONCLUSION

Since the New Order government of Indonesia came to power, the U.S. provided the largest share of total foreign

⁵¹ "Acungan Jempol bagi Kebijakan Makro" (Prize for Macro Policies), Tempo, 10 Juli 1993, p.72.

aid Soeharto administration received. The U.S. aid inflows could be regarded as "reward" for the Soeharto administration whose political orientation tends to be pro-Western. Geographically, Indonesia has strategic meaning in the context of global containment policy pursued by the U.S. Having failed in Vietnam (or Indochina as general), the U.S. did not want to see the "domino theory" work in neighboring countries. Therefore, when an Anti-Indonesian, leftist dominant group, called Fretilin, proclaimed East Timor as an independent country, the U.S. enthusiastically supported the Indonesian invasion in the second half of 1970s. The U.S. ODA inflows at that time demonstrated a relative increase. The U.S. did not want to see a Communist country exist in the middle of Indonesia.

Indonesia benefitted by the intense ideological conflict between Communism and the Western bloc in the region. Since the late 1970s, U.S. political security considerations have been directed to the Middle East (including Persian Gulf) area in which the "hot war" could easily erupt. Meanwhile the political stability of Indonesia appears assured, accompanied by steady economic growth. These conditions explain the falling of the U.S. ODA inflows in this period.

For the future, there is no reason the trend of U.S. ODA inflows will rise. Some factors which support this argument are as follows. As the Cold war era draws to an end, the political security justification of aid disbursement loses its

base. The U.S. balance of payments has been relatively high deficit, accompanied by the problems of unemployment and inflation at home. It makes the U.S. not only adjust her trade relationship with her large trading partners in the region such as Japan and NICs but also to cut off ODA in real terms. The "old" dimensions, such as human rights and support of democratic values, which were always overshadowed by a security justification, will be apparently accentuated in the future of the aid program. U.S. ODA inflows to Indonesia will not be exempt from such conditionalities. From the side of Indonesia, Soeharto regime can maintain the steady economic growth and domestic political stability. This good economic and political performance also becomes a factor which contributes to the declining of the U.S. aid inflows to Indonesia.

Only if there is a dramatic political change in Indonesian politics which is deemed able to unexpectedly disturb the stability in the region, will U.S. ODA inflows be higher than at the present. The only reasonable feature of financial transfers to Indonesia in the years to come will be in terms of commercial loans, foreign direct investment, and other such issues of economic interest to the U.S.

CHAPTER IV

THE POLITICS OF AID: JAPAN - INDONESIA RELATIONS

A. INTRODUCTION

As a donor country, Japan is in many ways quite different from the U.S. With her Marshall Plan, as described in the preceding chapter, the U.S. was a pioneer in evolving the practice of foreign aid as we understand it now. Japan, on the other hand, is a latecomer in the club of donor countries, as a result of the U.S.' pressure through San Francisco peace treaty. Unlike the U.S., Japan arose from the devastation of World War II on the strength of aid from other countries and international organizations before becoming the largest donor for 25 nations in the Developing world.¹ As a country in the losing side of the War, Japan is restricted from developing its military capability. This condition, in turn, influences its policy and practice of foreign aid. Almost all scholars studying Japanese aid program say that for more than two decades Japan did not have an aid philosophy. In fact, Japan

¹ Japan once was one of the largest recipient of foreign aid (the second, after India) from the World Bank. The last payment of the financing from the Bank was in 1989. For the list of the countries which receive ODA from Japan as the largest of their donors, see Yasutomo, Dennis T. (1989-90), "Why Aid? Japan As An 'Aid Great Power'," Pacific Affairs, Vol.62 No.4, Winter, p.490.

ties aid to its economic interests such as opening the markets for their products abroad, developing their business interests by investing in the recipient countries, and securing natural resource supplies from the Developing countries. Until the last decade, the appearance of Japanese foreign aid was one dimensional, driven by an economic rationale. In addition, only recently does Japanese aid go beyond the Asian border, although it is still concentrated in Asian countries. Of the ten largest recipient of its ODA, only one, i.e. Turkey, is not from Asia.

Problems in the way Japan disburses its aid are compounded by the quantity and the quality of its aid. In 1991, the share of Japan's Official Development Assistance (ODA) to Gross National Product (GNP) was 0.32 percent, slightly below the DAC average of 0.35 percent. It ranks the sixteenth of 18 donor countries. In terms of quality, the aid from Japan is considered as less concessional than that from other Development Assistance Committee (DAC) countries'. This figure is of course unexpected, coming as it does from a donor which enjoys relatively stable economic growth and a persistent trade surplus. Therefore, many have expected more from Japan in improving her aid program. The expectation is in fact supported by recent statistics on Japan's foreign aid which in 1988 and 1989 temporarily surpassed that disbursed by the U.S. In the years ahead, Japan will be under increasing pressure not only in terms of enlarging the total amount of

aid but also in terms of improving the concessionary part of it. At the same time, the orientation and rationale of its aid program are under strong criticisms.

Since the New Order government of Soeharto came to power, Japan has played a significant role in propping up financially Indonesia's economic development program. It was Japan which firstly appealed the Western donor countries to come together to discuss Indonesia's debt rescheduling. This effort continued to the creation of Inter Governmental Group on Indonesia (IGGI), as explained in chapter two. Actually, Indonesia has been the largest recipient of Japan's ODA for more than three decades and only some time in the 1980s was its position taken place by other Asian countries. Since 1974, Japan has been the largest donor for Indonesia, replacing the U.S.

We argue that Japan has been providing a significant amount of aid to Indonesia because Indonesia geographically and demographically can serve to fulfil Japan's economic interests, and in fact has done so. Indonesia has been supplying natural resources, such as oil, Liquid Natural Gas (LNG), timber, iron ore, and aluminum, needed for Japan's industries. Indonesia is in a strategic position, lying between two oceans (the Indian and Pacific) through which passage is made to and from Japan. Together with neighboring Malaysia and Singapore, Indonesia controls the Strait of Malacca and the Straits of Sunda and Lombok. These three

straits are passageways for vessels that come and go to Japan. With nearly 190 million people, Indonesia is also regarded as a huge potential market for Japan's industries.

This chapter will be divided into five sections. Section A is an introduction. Section B will examine the evolution of Japan's foreign aid program. This section will look at the continuity and improvement of Japan's aid program. The mechanism of aid policy-making and the way it is disbursed will also be briefly reviewed. Section C will review the implementation of aid policy in the context of Indonesia. This section will interpret the trends of Japan's aid inflows to Indonesia. Section D will propose some possibilities of Japanese aid to Indonesia in the years ahead. The conclusion will be given in the last section.

B. EVOLUTION OF JAPANESE AID PROGRAM

Japan provided foreign aid for the first time in early 1950s, although some scholars mention that the Japanese ODA program began in earnest in 1960s.² The concept "foreign aid"

² Prominent scholars such as Okita, Caldwell, Rix, and Hasegawa date the first Japanese foreign aid practice in early 1950s at the time the Export-Import Bank of Japan was established (1950) and the first reparation payment was concluded (1954). Whereas Yamaguchi, the chairman of Japan's Overseas Economic Cooperation Fund (OECF), argues that Japan "became a true donor nation" not until mid-1960s. This argument is based on the year of the creation of OECF of 1961 and the initiatives originated from Japan herself to disburse

itself in the first decade of Japan's aid program did not come explicitly as the one which should be dealt with seriously and independently. The program of aid was always included in the larger concept of "economic cooperation" encompassing other elements such as trade and investment. Before examining the evolution of the Japanese aid program, it is noteworthy to mention some features of the program.

First, the Japanese government's aid program does not seem to go along with a humanitarian point of view. It is not inspired by a motive to contribute to global prosperity or the moral principle that rich countries should give assistance to poor countries. There is a tendency for Japan to disburse its foreign aid because of external pressure, i.e. all the other developed countries have undertaken such a program. "Aid seems to be as little more than the price of admission to the club of rich countries," one Japanese scholar, Koichi Mera, acknowledges.³

This assertion is supported by three conditions. First, The level of Japan's ODA as a percentage of GNP is always low. It was never beyond a ratio of 0.29 percent, well below the DAC average of 0.35 percent. Only recently, since 1987, has the ratio gone beyond 0.30 percent, but it remains below the

aid, instead of the disbursement of externally pressured reparations payment. See the interview with Yamaguchi in "Directing Japan's Aid Efforts", Japan Echo, Vol.XVI, No.1, Spring 1989, pp.8-12.

³ Mera, Koichi (1989), "Problems in the Aid Program," Japan Echo, Vol.XVI, No.1, Spring, p.13.

DAC average. Second, Japan is stingy in term of the "grant element". For the last ten years, it is only 66.8 percent, the lowest among 18 DAC countries, whereas the average for DAC countries is 93.2 percent. Third, Japanese aid is heavily "tied" to purchases from Japanese suppliers. It is commonly known that "companies in other countries have a hard time participating in the business generated by Japan's grant and loans even when this aid is untied."⁴

The second prominent feature of Japan's aid program is that in disbursing its aid, Japan concentrates geographically in Asia, and most of it goes to the Southeast Asian countries. Since 1970-71, Four Association of South East Asian Nations (ASEAN) countries, namely Indonesia, the Philippines, Thailand, and Malaysia, have enjoyed the lion's share of Japan's ODA. In 1990-91 the geographic total gross disbursement of ODA in percentage terms is as follows. Sub-Saharan Africa received 11.5 percent of the total. Asia received the lion's share, 68.5 percent. The Middle East and North Africa received 11.7 percent, while Latin America and the Caribbean received only 8.3 percent. Of the ten largest recipient countries, only one two countries are not from Asia: Egypt in 1980-81 and Turkey in 1990-91. As recipients of Japanese ODA, they are ranked eighth and seventh

⁴ Ibid, p.14.

respectively.⁵ The geographical concentration of aid disbursements is not merely driven by the neighboring region and historical (colonial) ties which exist between Japan and the Asian recipients. The pattern of aid relations is largely influenced by or in accordance with Japan's pursuit of economic capitalism. These countries are regarded as both a market and as natural resource suppliers for Japanese industries. As a resource-poor country, Japan heavily depends on imports from these countries to run its industries, as recognized by the chairman of Overseas Economic Cooperation Fund (OECF), "Japan can't live in isolation from international society; our country depends on other countries for survival."⁶

Third, Japan prefers to disburse project aid to program aid. This is so because ODA is defined as a tool to encourage private investment by providing infrastructure.⁷ As comparison, in 1975-76 Japan's aid disbursed for infrastructure uses accounted for 40 percent and the share of program assistance was only 0.1 percent. In 1989-90, infrastructure-related aid became 51 percent of total ODA

⁵ Organization for Economic Cooperation and Development (OECD) (1992), Development Co-operation, 1992 Report, Paris: OECD, p. A-18 & A-60.

⁶ "Directing Japan's Aid Efforts," Op Cit, p.8.

⁷ Healey, Derek (1991), Japanese Capital Exports and Asian Economic Development, Paris:OECD, p.106.

disbursements and program assistance jumped to 19 percent.⁸ Critics of Japan's ODA assert that in disbursing its aid, Japan traditionally has focused on growth with scant attention to poverty.⁹ Japan's ODA is heavily disbursed for projects on the basis of cost-benefit analysis, ignoring the human aspects. Japan concentrates on big-scale projects which provide quick-benefits for Japanese business and industry, neglecting the basic human needs of people. They dub Japanese ODA as "Official Destruction and Alienation".¹⁰

Japan also gives less technical assistance. Its share in Japan's ODA disbursed in 1989-90 averaged only 13.7 percent, far below the 21.0 percent DAC average in the same period. Its position is twelfth of 18 DAC countries. The main reason for this is that technical assistance is not commercially attractive. When ODA is directed towards technical assistance, much of the expenditure will go to pay technicians. In fact, a large portion of the cost of financial aid goes towards materials and machinery because it commercially benefits Japanese economy. This reason is coupled with a lack of linguistic capability of Japanese experts. On this situation,

⁸ OECD (1992), Op Cit, p.A-19.

⁹ Lewis, John P. (1993), Pro-Poor Aid Conditionality, Policy Essay No.8, Washington, D.C.: Overseas Development Council, p.38.

¹⁰ Schultz, Richard W. (1991), "Japan's ODA: The Blessings and the Bane," Tokyo Business Today, September, Vol.59, No.9, p.12.

a report of the Joint Economic Committee of the U.S. Congress
comments:

Externally...Japan has continued to give less priority to areas without commercial rewards. Among industrial nations it ranks near the bottom in terms of the share of its resources devoted to...development assistance. To the extent that Japan has provided development assistance, it has had a reputation for tying and to purchase of Japanese exports.¹¹

Fourth, Japan's aid program is a result of interaction between government agencies and private entities.¹² In the implementation of aid policy, Japan also relies not only on her public institutions and agencies for capital and technical assistance activities, but also on private business for the provision of credits and investments. There are four ministry agencies acting as decisive actors in the process of foreign aid policy formulation in Japan. They are directly involved in deciding every single yen that Japan disburses. As a result, it is quite often that the aid process is characterized by frequent interministerial conflict of interests.

¹¹ As cited by Healey (1991), Op Cit, p.108. from Joint Economic Committee (1988), Restoring International Balance: Japan's Trade and Investment Patterns, Washington, D.C., 1st July, p.37.

¹² For good and comprehensive discussion on how foreign aid policy is made in Japanese politics, see Rix, Alan (1980), Japan's Economic Aid, Policy-Making and Politics, New York: St. Martin's Press.

The Ministry of Foreign Affairs (MFA, or *Gaimusho*) acts as the "window" for aid through which all request must be channeled. The forum of the four-ministry group is chaired by the ministry. It also has authority to supervise technical assistance activities and disbursement of grant aid. The main interest of the ministry, in the context of aid disbursement, is to foster stable political relations between Japan and the Third World. The Ministry of Finance (MOF, or *okurasho*) exercises considerable influence through its budget-making authority. The Ministry of International Trade and Industry (MITI, or *tsusansho*) stresses the commercial aspect of foreign aid. The last ministerial agency is the Economic Planning Agency (EPA) which emphasizes on the implication for Japan's economic prospects. This agency is legally in charge of controlling the activities of ODA disbursement. In addition to the above government agencies, certain prominent members of *zaikai*, the business world, also play a significant influence during the preparation stage of aid formulation and implementation.¹³

On the side of foreign aid program implementation, there are four institutions each with a specified domain. The Japan International Cooperation Agency (JICA), under MFA, handles technical assistance and grants. The Overseas Economic Cooperation Fund (OECF) is in charge of disbursing development

¹³ Hasegawa, Sukehiro (1975), Japanese Foreign Aid, Policy and Practice. New York: Praeger Publishers, p.131.

assistance (ODA). The Export-Import bank of Japan is responsible for providing loans at near-commercial rates to recipient countries. The last agency is the Japan Overseas Development Cooperation (JODC), whose main task is to promote industrial development and trade in Developing countries by providing required capital for joint-ventures carried out by small and medium-sized Japanese companies.¹⁴

Compared with the U.S., Japan relies more on the private sector to implement its aid program. This is reflected in the total number of aid personnel stationed abroad. In 1988 the Japanese government employed 357 personnel abroad to administer aid program related activities. This contrasted with U.S. AID which stationed 1,275 American personnel abroad and recruited 1,170 foreign nationals for its operations. The comparison is also relevant in the case of Indonesia. In 1987, Japan posted 26 aid professional in Indonesia to handle over \$700 million in Japanese aid. In the fiscal year (FY) 1989 AID employed 41 Americans and 69 Indonesian people to run a program of a little more than \$57 million.¹⁵

Fifth, Japanese foreign aid has consistently appeared for more than three decades with its one-dimensional "face". More than 15 years ago, Hasegawa argued that "Japanese aid is seen as an instrument of Japan's national policy to serve the

¹⁴ Healey (1991), Op Cit, pp.126-30.

¹⁵ Orr, Robert M. (1989-90), "Collaboration or Conflict? Foreign Aid and U.S. - Japan Relations," Pacific Affairs, Vol.62 No.4, Winter, p.481.

kokueki, or national interest, of 'secularized postwar Japan'.¹⁶ What is the national interest of "secularized postwar Japan" is economic interests. Aid disbursement has been always driven by economic interests and even it seems that until now those motives are still dominant. Japan extends aid as a means of increasing its exports, securing adequate supplies of natural resources, and creating conducive conditions for private investment in the recipient countries. As Orr puts it, Japanese aid is exercised "as an extension of the notion of Japan Inc. Aid is linked to investment and trade, as a means to promote overseas commercial interests."¹⁷

Historically, Japan's aid policy can be divided into five stages or periods.¹⁸ It should be borne in mind that when we divide the evolution process of Japanese foreign aid policy into five stages or periods, one stage encompasses a certain period of time and the period will overlap with the next

¹⁶ Hasegawa (1975), Op Cit, p.7.

¹⁷ Orr (1989-90), Op Cit, p.447.

¹⁸ Caldwell, Hasegawa, Orr, and Okita have made the periodization of Japanese aid policy history. In making the phases of the history, each has a slightly different opinion. See Caldwell, J. Alexander (1972), "The Evolution of Japanese Economic Cooperation," in Malmgren, Harald B. (ed.), Pacific Basin Development: The American Interests, Lexington, Massachusetts, D.C.: D.C. Heath and Company, pp.31-45; Hasegawa (1975), Op Cit, pp.11-23.; Orr, Robert M. (1987), "The Rising Sun: Japan's Foreign Aid to ASEAN, the Pacific Basin and the Republic of Korea," Journal of International Affairs, Vol.41 No.1, Summer/Fall, pp.39-62.; Okita, Saburo (1990), Approaching the 21st Century: Japan's Role, Tokyo: The Japan Times, Ltd., pp.101-5.

stage. Through the evolution of foreign aid policy initiatives or formulation, we find a prevailing consistency in the motive or rationale behind Japan's provision of aid in every stage or period, i.e. for the sake of its economic interests. This does not mean that there are no other dimensions, such as the political and strategic. These come later in the evolution process, but both dimensions are subordinate to the economic one. They serve to keep or secure and promote Japan's economic interests.

In the following paragraphs, we would like to make the division of Japanese aid policy as follows. Stage one is "Reparations payment" which lasts from 1955 to early 1970s. Stage two, from 1960 to 1973, is the period when aid is used as a means of its Asian Diplomacy, in the search for natural resources, besides the promotion of exports. In stage three, inspired by the first oil price hike, aid is directed to resource-rich countries and nations located on energy shipping routes. Stage four occurs in 1980s, when the political and strategic dimensions come up to supplement in foreign aid program. The last stage appears after the end of the Cold War era, in the late 1980s and early 1990s.

1. STAGE ONE: REPARATIONS PAYMENT, 1955-EARLY 1970s

The reparations payment initiatives that Japan's government took are all directed towards the neighboring Asian

countries as a compensation of suffering they got when Japanese colonial rule occupied their territories before the end of the World War II. Japan first concluded a reparation (*baisho*) agreement with Burma in 1955. In subsequent years, Japan also provided reparations and quasi-reparation (grants in lieu of formal reparation commitments) payment to the other neighboring countries such as the Philippines (1956), Indonesia (1958), Laos and Cambodia (1959), (South) Vietnam (1960), Thailand (1962), South Korea and Burma (1965), Singapore and Malaysia (1968), and Indonesia (1972).¹⁹ The total amount disbursed for *baisho* and economic grants accounted for a little more than \$1.5 billion.²⁰

In the 1950s, Japan allegedly had not yet evolved its specific aid policy. Even the word or concept "aid" did not exist in its official political agenda. Instead, the larger concept "economic cooperation" had been introduced in December 1953 by Yoshida Cabinet. The principles involved are as follows,

1. Japan will respect the position of the countries to which it gives assistance and positively cooperate in related plans by a third country or the U.N. in promoting economic cooperation with Asian nations.
2. The economic cooperation will be done on the basis of the creative will of private enterprise in principle, and the government will provide necessary assistance to carry out the project.

¹⁹ Rix (1980), Op Cit, p.33.

²⁰ Hasegawa (1975), Op Cit, p.28.

3. Japan will try to settle with the countries with which it has reparations problems as quickly as possible.²¹

In a later semi-official document of 1959, it is clear that economic cooperation encompasses reparations, direct private investment, yen credit, deferred payment, and technical cooperation.²²

The 1958 White Paper on Economic Cooperation published by MITI was quite specific. It stated that economic cooperation was to serve two objectives: to keep the market for Japanese export commodities stable and to secure supplies of raw materials. To these ends, the Japanese government encouraged the private enterprises actively involved in the program.²³ This condition is reflected in the practice of reparation grant disbursements. The government did not take part directly in this program. Private business handled this on behalf of the government. The mechanism went as follows. The list of projects whose financing comes from the reparation money was proposed by the recipients to be approved by Japanese government. When approved, the recipient government offered the projects to Japanese private businesses and negotiated with them its implementation. This method is regarded as a successful means of making Japanese business familiar with the

²¹ Caldwell (1972), Op Cit, p.27.

²² Ibid, p.27.

²³ Ibid, p.29

situation of the recipient countries and in turn opening prospective market for their products there.

Economically, *baisho* were utilized to help Japan's economic recovery, to promote its export, and to facilitate heavy industrialization at home. Politically, the initiative to pay *baisho* was made to establish diplomatic ties between Japan and neighboring countries, as an essential step towards Japan's reentry into the international community. Once such diplomatic ties are forged, Japan's economic interests are protected and advanced.²⁴ Because of the nature of these reparation payments, it is hard not to judge Japanese aid as self-oriented. As Okita realized: "...there was a conscious policy decision made in this stage not to inquire whether or not the funds were actually contributing to the recipient country's economic development."²⁵

Although criticisms of Japanese foreign aid strongly prevails, it is not easy to blame Japan for her heavy trade orientation in the first two decades of its program. With a per capita income of only \$357 in 1958²⁶ and persistent

²⁴ Masogawa (1975), Op Cit, p.38-44.

²⁵ Okita (1990), Op Cit, p.101.

²⁶ This economic indicator actually makes Japan entitled to receive aid. One of the factors explaining Japan's disbursements of aid in this period is U.S. pressure, reflected in the San Francisco Peace Treaty signed on September 8, 1951.

balance of payment problems²⁷, it seemed to be unrealistic to expect more. The main problem Japan had to deal with was its own economic survival and growth.

2. STAGE TWO: AID WITHIN ASIAN DIPLOMACY, 1960-73

As explained above, some argue that the truly Japanese aid program began in this period. It can be understood because in this period, Japan started evolving aid institutions and aggressively demonstrating its aid diplomacy. Initiated on becoming a member of the OECD's Development Assistance Committee (DAC), Japan set up in March 1961 its OECF under the ministry of EPA, which was responsible for providing long-term and low-interest capital assistance (ODA) to the Developing countries. In the following year, June 1962, Overseas Technical Cooperation Agency (OTCA) was created to execute official technical cooperation activities.

In the diplomatic scene, Japan around 1965 began to actively integrate its "economic cooperation" principle into Japan's Asian foreign policy. The statistical figure of ODA disbursement illustrates this step. In 1963, Of the total ODA

²⁷ Until 1965, Japanese trade continuously suffered from a deficit *vis-a-vis* its trading partners. See, Hasegawa (1975), Op Cit, table 6.1., p.79.

disbursed by Japan, 98.7 percent was directed towards Asia²⁸, whereas in 1969 almost 100 percent of its ODA was disbursed in Asia, 48.5 percent of it in Southeast Asia. Economic Cooperation agreements were reached with Taiwan and Korea, and Japan was actively involved in the creation of Asian Development Bank (ADB) in 1966.²⁹ Japan also hosted the ministerial conference for the Economic Development of Southeast Asia and the first meeting on Indonesia's debt scheduling arrangement. From the inception of IGGI through early 1970s³⁰, Japan shouldered the burden for one-fourth of the foreign credits extended to Indonesia and since then Indonesia has always been receiving the lion's share of Japanese aid.

These conscious steps cannot be separated from Japan's intention to double its per capita income through the so-called "income-doubling plan" during the 1960s.³¹ To materialize this plan, Japan redesigned its aid program. Japan

²⁸ Rix (1980), Op Cit, p.33.

²⁹ For the comprehensive study on the topic, see Yasutomo, Dennis T. (1983), Japan and the Asian Development Bank, New York: Praeger Publishers.

³⁰ Over the same period, the U.S. provided about 40 percent of total assistance channeled through IGGI. On this, see chapter three.

³¹ Hasegawa (1975), Op Cit, p.78. In fact, by the end of 1960s, Japan had achieved the world's third largest GNP and had become one of the few countries persistently registering a trade surplus since 1965 until the oil price hike of 1973 again hit its trade balance.

developed its *kaihatsu yunyu* ("development-cum-import") scheme. According to this scheme, Japan would extend capital and technical assistance to develop and process natural resources in recipient countries for their export either to Japan or other countries. To enhance the scheme, Japan in February 1970 set up the Overseas Trade and Development Association (OTDA) charged with the responsibility of extending funds for the construction of physical and social infrastructure directly related to the production of primary commodities. In this context, it seems no exaggeration to say that the practice of "development-cum-import" scheme involves "the exploitation of energy and mineral resources"³² of the recipient countries for the sake of the security of Japanese vital energy resource and raw material supplies.

3. STAGE THREE: AID FOR SECURING NATURAL RESOURCES SUPPLIES, 1973-EARLY 1980s

The oil price crisis of 1973 demonstrated how dependent upon the natural resources supplied from the Developing countries Japan's economic viability is. This event also taught Japan a valuable lesson that aid can be used effectively as a diplomatic tool beyond Asia. Before the oil crisis, nearly 100 percent of Japanese ODA flowed to Asian

³² Ibid, p.80.

countries. Japan began directing its ODA to natural-rich countries and the countries which are located on energy-shipping routes.

At the first oil crisis of 1973, Japan disbursed ODA both bilaterally to the Developing countries and through multilateral institutions almost double than that of the preceding years. In 1972, Japan disbursed ODA of around \$611 million and in 1973 little over \$1 billion. This increase, of course, made the percentage of ODA disbursements against its GNP jump from 0.20 percent to 0.25 percent. This percentage was still far below from the ideal target of 0.7 percent desired by the U.N. and accepted by Japan and even still less than percentage of the DAC average. Yet when compared with the total ODA disbursed by the U.S., it indicates a quite dramatic increase. At the same time the U.S. cut its ODA up to one-third, from \$3.9 billion in 1972 to \$2.6 in the following year. As a consequence, its ODA share against its GNP slid from 0.33 to 0.20 percent. The factors causing this fall, as explained in chapter three, were "aid fatigue" of the American people and their frustration about Vietnam. The average percentage of DAC countries also fell from 0.35 to 0.29 percent (See table 4.1.).

The same increase of Japanese ODA reoccurred in the second oil crisis in the late 1970s. Again in total terms, in the ODA disbursed both bilaterally and through multilateral institutions, in three consecutive years from 1978 to 1980,

Japan increasingly extended aid from \$2.2, \$2.7, to \$3.4 billion. This meant that its ODA as a percentage of GNP increased from 0.23 to 0.27 and 0.32 percent respectively.

In this period, Japan also recorded an improvement of its ODA quality. As a comparison, the terms of Japan's ODA in 1960s was as follows. Its interest rate was 5.25 to 5.50 percent; the maturity period was 15 years, with five years as a grace period. In contrast, the composition of its ODA terms and condition in 1970s for the same items was respectively 3.5 percent, 20 years, and 6-7 years. The new procedure of technical assistance activities was introduced by establishing Japan International Cooperation Agency (JICA) which is in charge for managing Japan's technical aid program, some development funding and assisting emigration in 1 August 1974. JICA has replaced the former institution OTCA. This move can be explained as Japan's accommodationist attitude in responding to the hostile feeling of people in some recipient countries. This hatred was expressed when Prime Minister Tanaka made his official visit to ASEAN countries in 1974. He was welcomed by the strong protest and demonstration of students, especially in Bangkok and Jakarta.³³

Despite such an improvement, Japanese aid quality, as described above, was still well below the average DAC

³³ In Indonesia, the of protest is usually called "Malari" (for *Malapetaka Lima belas Januari*, or literally Disaster of January the fifteenth) event of 1974 which caused both material and life loss.

countries. As an example, only 5 percent of 1977 aid was in the form of grants to multilateral agencies, compared with the DAC average of 15 percent. It is "Japanese business" rather than "poverty need" which is still predominant in determining aid allocation.

4. STAGE FOUR: POLITICAL STRATEGIC DIMENSIONS, LATE 1970s-EARLY 1990s

The initiative to use aid as a means for achieving political and security objectives as well as economic benefits initially came up in the second half of 1970s. Over this period, external political conditions were so vulnerable that Japan should take measure to secure its economic benefits. Saigon completely fell down. The Indochinese region was seized by Communist forces. The Soviet Union invaded Afghanistan. The Iranian hostage crisis erupted and there was a second oil crisis. Constitutionally, Japan is prohibited from exercising any military role in securing international peace and stability. Japan's military is allowed for self-defense. Because of these conditions, Japan sees its ODA as an alternative means Japan can use in participating in the efforts of maintaining international stability.

Japan recognizes that economic and social stability in the Developing countries cannot be separated from the maintenance of world peace and stability. Regarding this condition, Japan realizes that its aid can be an important

element to support world security. As of this period, Japan's government has begun to seriously evolve a series of medium-term plans to guide the expansion of its ODA program.³⁴ The first plan, adopted in 1977, was intended to double the annual value of aid to \$2.8 billion in the 1978-1980 period. This goal was fulfilled and in fact, in 1980, the total disbursed aid reached \$3.3 billion (see table 4.1).

Under PM Masayoshi Ohira (1978-80), the Japanese government for the first time deliberately attached political and strategic conditions to the use of foreign aid by pledging more aid to "countries bordering conflict" (limited to Thailand, Pakistan, and Turkey). It canceled aid to Vietnam and initiated aid to China in 1979-80.³⁵ Although the steps taken by Japan to increase its aid disbursement is to some extent caused by external pressure as a compensation for its limited burden sharing of international defence³⁶, the

³⁴ For a good discussion on the series of medium-term plans, see Sudo (1989), "Japan's Role in the Context of the Emerging Asia-Pacific World," in Southeast Asian Affairs 1989, Singapore: Institute of Southeast Asian Studies, Boulder, Colorado: Westview Press, pp.51-65.

³⁵ Yasutomo (1989-90), Op Cit, p.494. For an excellent discussion on the attachment of strategic dimension into Japanese ODA program so far, see Yasutomo, Dennis T. (1986), The Manner of Giving, Strategic Aid and Japanese Foreign Policy, Lexington, Massachusetts: D.C. Heath and Company.

³⁶ The Western donors also criticize the pattern of Japanese ODA disbursement which follows such a rule as 70-10-10-10, that is, 70 percent is directed to Asia and each of the other tens are for Africa, Middle-East, and Latin America. Japan is encouraged to widespread its aid geographically. See, Orr, Robert M. (1988), "The Aid Factor in U.S.-Japan Relations," Asian Survey, Vol.XXVIII, No.7, July, p.754.

government's initiative to disburse more aid seems to be supported by its constituents. Public opinion polls conducted during the years 1977 to 1981 demonstrated that the foreign aid program was registered to have a consistent 75 to 80 percent support rate.³⁷ This support reflects the realization of the Japanese that their country's economic survival depends on the supplies of natural resources which Japan itself does not have.

In December 1980, Prime Minister Zenko Suzuki adopted "Comprehensive National Security" as a national policy. The stress on "economic cooperation" in this policy refers to military means of pursuing national security.³⁸ In the area of aid, this policy endorses the practice of "Aid for countries bordering on areas of conflict" pursued by P.M. Ohira. In this year, the second medium-term plan was acknowledged. This plan was aimed at providing aid worth \$24 billion in the period from 1981-1985, double the amount of the assistance extended in the 1976-1980 period. Yet this goal was not achieved. The total amount of aid disbursed at that period, in fact, reached only \$18 billion.

³⁷ Yasutomo (1986), Ibid, p.3.

³⁸ See Akaha, Tsuneo (1991), "Japan's Comprehensive Security Policy, A New East Asian Environment," Asian Survey, Vol.XXXI, No.4, April, pp.324-40. Actually, the concept "Comprehensive National Security" was developed by a study group which was deliberately created to discuss and formulate the issue. The group was established by P.M. Ohira in 1979 and comprised of academics, businessmen, and government officials.

**Table 4.1.: Comparison of Total Net ODA from U.S. and Japan
and Their ODA as Percentage of GNP**

Years	Total U.S.' disbursed ODA	As % of GNP	Total Japan's disbursed ODA	As % of GNP	DAC Average
1969	3,376	0.36	436	0.26	0.37
1970	3,153	0.32	458	0.23	0.34
1971	3,112	0.29	511	0.22	0.33
1972	3,958	0.33	611	0.20	0.35
1973	2,655	0.20	1,011	0.25	0.29
1974	3,673	0.25	1,126	0.25	0.33
1975	4,160	0.27	1,148	0.23	0.35
1976	4,360	0.25	1,105	0.20	0.33
1977	4,682	0.24	1,424	0.21	0.33
1978	5,664	0.27	2,215	0.23	0.35
1979	4,684	0.20	2,686	0.27	0.35
1980	7,138	0.27	3,353	0.32	0.37
1981	5,782	0.19	3,171	0.28	0.35
1982	8,202	0.27	3,023	0.28	0.38
1983	8,081	0.24	3,761	0.32	0.36
1984	8,711	0.24	4,319	0.34	0.36
1985	9,403	0.24	3,797	0.29	0.35
1986	9,564	0.23	5,634	0.29	0.35
1987	9,115	0.20	7,342	0.31	0.34
1988	10,141	0.21	9,134	0.32	0.34
1989	7,676	0.15	8,965	0.31	0.34
1990	11,394	0.21	9,069	0.31	0.35
1991	11,262	0.20	10,952	0.32	0.33

Source: OECD (1985), Twenty-Five Years of Development Cooperation, Paris: OECD, pp.334-5. and OECD (some issues), Development Cooperation, Annual Report, Paris: OECD.

The third plan was initiated in September 1985. Under this plan, the government intended to extend more than \$40 billion during the seven-year period until 1992. In the same month, as a result of "Plaza Agreement"³⁹, the value of Yen climbed up against the U.S. dollar. Because of the Yen's appreciation, the ODA budget for 1986 was raised to 52 percent in Dollar terms, although in Yen terms it was hiked by only 7 percent. In 1987 it was similar. A rise of just under 6 percent in Yen became a 23 percent Dollar increase.⁴⁰ In the three consecutive years after 1985, ODA jumped up from \$3.8 billion in 1985 to \$5.6, \$7.3, and \$9.1 billion respectively (see table 4.1). This situation made it obvious that this goal would be achieved well ahead of schedule. Therefore, the fourth plan was developed before Japan came to the Toronto summit of the Industrialized economies in June 1988.

In May 1988 P.M. Noboru Takeshita announced an "International Cooperation Initiative". By acknowledging the initiative, Japan intended to demonstrate its intention of promoting peace and international prosperity to international community. The initiative was based upon three pillars: (1)

³⁹ The "Plaza Agreement" was reached in New York in September 1985. All finance ministers of the major industrialized countries agreed to bring about a weaker dollar and a strong yen. The Yen since then has risen from a value of Y260 to the dollar to about Y125 to the dollar. See, Ping (1990), "ASEAN and the Japanese Role in Southeast Asia," in Broinowski (ed.), ASEAN Into the 1990s, New York: St. Martin's Press, p.167.

⁴⁰ Motoo (1989), "Foreign Aid: A Dissenter's View," Japan Echo, Vol.XVI, No.1, Spring, p.20.

strengthening of Japan's contribution to international peace. (2) expansion of ODA, and (3) promotion of international cultural exchange.⁴¹ To implement the initiative, in the June 1988 Toronto summit of the industrialized countries, Japan acknowledged its fourth medium-term plan which aimed at doubling the ODA extended over the 1983-1987 period to at least \$50 billion in the five years from 1988 through 1992.

In 1989, Japan temporarily became a largest donor. The total amount of ODA disbursed by Japan surpassed that of the U.S., i.e. \$9.6 billion versus \$7.6 billion (see table 4.1.). Unlike the controversial nature of the military budget, the ODA program still enjoyed great support from the people. A survey conducted by P.M.'s office at the time shows that 42.4 percent of the respondents approved of the amount, 39.4 percent supported a larger amount, 8.2 percent preferred a smaller amount, and 1.2 percent wanted an end to all ODA.⁴²

5. STAGE FIVE: SEARCHING FOR A NEW AGENDA IN POST COLD WAR ERA

When the Cold War ended, the economy of Japan came up as the most steady among the industrialized countries. During the years 1980-91, the Japanese economy grew at 3.6 percent average annually, while the U.S.' economy over the same period

⁴¹ Akaha (1991), Op Cit, p.328.

⁴² Ibid, p.332.

grew only 1.7 percent. Other indicators such as the inflation rate, the unemployment rate, and the Current Account demonstrates the relative strong position of Japanese economy against that of the U.S. The table of economic indicators below illustrates the solidity of Japanese economy, compared with the U.S.' Even since 1980, Japan has enjoyed a persistent dramatic surplus against its trading partners. Its trade balance shows a continuing surplus, except in 1982 when the Japanese surplus slightly decreased from the preceding year although the figure was still dramatic. The figure of trade balance, from 1980-88, went as follows (in US\$ billion): 2.1; 19.9; 18.0; 31.4; 44.2;

Table 4.2.: Economic Indicators for Japan and the U.S.

	JAPAN	U.S.
GNP Per Capita 1991 (in U.S. Dollar)*)	26,930	22,240
GNP Annual Average Growth Rate, 1987-90	5.2	3.6
Inflation Annual Average Rate, 1980-91	3.6	1.7
Unemployment Rate in 1990	2.1	5.5
1989 Budget, Surplus (+) or Deficit (-) as % of GNP	(+) 2.5	(-) 1.7
Current External Balance, % of GNP 1990	1.2	-1.8
Total Government Outlays as % of GNP 1989	32.9	36.9

Source: OECD (1991), Development Cooperation, 1991 Report, Paris: OECD, p.184.

*) Taken from World Bank (1993), World Development Report 1993, Washington, D.C.: IBRD.

55.9; 92.8; 96.3; 95.0 respectively.⁴³ As of the last decade, Japan has become a country with a great capital surplus. Therefore, Japan is encouraged to recycle its capital surplus for the Developing countries, in term of grant or soft loans.⁴⁴

The external pressure for Japan to disburse more aid becomes apparent in the period of the post-Cold War era. Robert McNamara, former president of the World Bank, argued that, with per capita income much higher than other industrialized countries, Japan should be the leader in extending ODA.⁴⁵ This assertion parallels Okita's idea,

It would be unreasonable to ask the Japanese people suddenly to raise their propensity to consume. It would be more feasible for them to channel a large fraction of their continued high savings into development assistance.⁴⁶

The Japanese ODA program has been so far under strong criticisms due to some factors, as explained above. Japanese

⁴³ See Katsuzo, Sakamoto & Richard C. Conquest (1992), "The Internationalization of Japanese Capital," in Hook, Glenn D. & Michael A. Weiner (eds.), The Internationalization of Japan, London & New York: Routledge, table 7.1., p.132.

⁴⁴ See Ozawa, Terutomo (1989), Recycling Japan's Surpluses for Developing Countries, Paris: OECD, for a good discussion on the topics.

⁴⁵ do Rosario, Louise (1992), "Help Those Who Help Themselves," Far Eastern Economic Review, 18 June, pp.58,60.

⁴⁶ As cited from Lewis, John P. (1987), Asian Development: The Role of Development Assistance, Lanham, New York, London: University Press of America with the Asia Society, p.42.

ODA has concentrated on infrastructure and production projects which bring about economic or commercial benefit for itself, neglecting social projects such as education, health, and population control. Japanese ODA consists more of loans than grants. Japan is still ranked the lowest of the DAC countries, with grants accounting for 43.2 percent of its total ODA, compared with the DAC average of 75.6 percent. Japan, in disbursing aid, is concerned with economic growth, rather than economic distribution.⁴⁷

Because of the strong criticisms, accompanied by the changing international political situation after the Cold War period, in October 5, 1992, the Japanese government issued a White paper on foreign aid which stressed that disbursement of ODA should be tied to the so-called Four Principles. The principles are that ODA disbursement should be linked to the recipient country's records on (1) military spending, (2) arms exports or sales, (3) democracy, and (4) market reforms.⁴⁸ Two major themes which get a great space in every public debate on Japanese aid both outside and inside the country are human rights and the environment.

In the near future, it seems that the Japanese ODA program will still facilitate its prevailing commercial or economic drives. It does not mean that we have a pessimistic

⁴⁷ Rowley, Anthony (1991), "Generosity Has Its Limits," Far Eastern Economic review, 20 June, p.63.

⁴⁸ do Rosario, Louise (1992), "Flexible Principles," Far Eastern Economic Review, 15 October, p.20.

view of the Japanese ODA program in the future. In fact, we believe that the post-Cold War concerns such as democracy, human rights, and environmental awareness will also become significant determinant in allocating Japanese ODA. Yet for Japan, to come to this situation is not an overnight process. It is so because the dependence of Japan upon the supplies of natural resources for its economic survival is so profound that its government will not let its economy slow down or be disturbed just for the sake of pursuing such ideas.

C. JAPANESE FOREIGN AID PRACTICES TO INDONESIA

1. FEATURES OF JAPANESE AID

As mentioned in the preceding chapters, when the New Order government of Indonesia came to office, Japan took the initiative to bring together Western donor countries and the Indonesian government to discuss debt rescheduling for Indonesia. Since then, Japan has extended a significant amount of aid to Soeharto's regime. Until 1982, Indonesia received the lion's share of Japanese aid. It was always ranked as the largest recipient, accounting for an average 15 percent of total ODA disbursed by Japan annually over that period of time (see table 4.3). From 1983 to 1986, Indonesia's position as

Table 4.3.: Japanese ODA to Indonesia
(in million US dollar and as % of total disbursed)

Year	Total ODA Disbursed by Japan	Japanese ODA to Indonesia	As % of Total
1969	436	65.8	15.1
1970	458	125.8	27.5
1971	511	111.9	21.9
1972	611	103.2	16.8
1973	1,011	142.9	14.1
1974	1,126	221.1	19.6
1975	1,148	197.9	17.2
1976	1,105	200.5	18.1
1977	1,424	148.4	10.4
1978	2,215	227.6	10.3
1979	2,686	226.9	8.4
1980	3,353	350.0	10.4
1981	3,171	299.8	9.5
1982	3,023	294.6	9.8
1983	3,761	235.5	6.3
1984	4,319	167.7	4.4
1985	3,797	161.3	4.2
1986	5,634	160.1	2.2
1987	7,342	707.3	9.6
1988	9,134	984.9	11.0
1989	8,965	1145.3	12.6
1990	9,069	867.8	9.6
1991	10,952	1065.5	9.7

Source: the same as tables 4.1. and 3.1. above.

the largest recipient country of Japanese ODA was temporarily assumed by China. Since 1987, Indonesia again has been receiving the largest amount of Japanese ODA.

In the first half of the 1980s, Japanese ODA extended to Indonesia tended to decrease continuously. It was along with the general trend of Japanese ODA disbursement in the first two years of 1980s, indicating slowing down and unstable. After value of the Yen was appreciated against the dollar in September 1985, Japanese ODA disbursement has demonstrated a significantly increasing trend, with the exception of 1989. In 1987, Japan provided ODA more than quadruple the amount of that extended a year earlier, from \$160 million to \$707 million, and since then Indonesia once again has been the largest recipient of Japanese ODA. Of that total amount, 60 percent was in the form of program lending for Indonesia's debt repayment.

Since the appreciation of the Yen, Indonesia's debt repayment obligation which was due at the time doubled.⁴⁹ This was because around 45 percent of Indonesia's foreign borrowing consists of Yen-denominated credits while most of its export earnings are in U.S. dollars. Therefore, Indonesia should spend more dollars in purchasing yen. This condition deteriorated Indonesian economy which had been hit by the

⁴⁹ Before 1985, Indonesia's debt repayment obligation was still \$2 billion per year and suddenly it soared at \$3-\$4 billion per year. See, "Experiment Mata Uang," (The experiment of Currency), Tempo, 17 Oktober 1992, p.91.

decline of export earnings from oil. The Indonesian government, through its then Minister of Finance Sumarlin, proposed to Japan that the repayment of the outstanding debts at the exchange rate prevailing at the time of their disbursement or before "Flaza Agreement". But the Japanese government quickly turned it down.⁵⁰ Indonesia also requested dollar-denominated loans from Japan but this request was also rejected by Japan.

It is quite interesting to take a look at the figure of aid disbursement in the year 1989. Japan was the largest donor of DAC members, surpassing temporarily the U.S. In fact, the total amount of ODA extended by Japan at the time declined from the preceding year, from \$9.1 billion in 1978 to \$8.6 billion of 1989.

At the same year, the total ODA disbursed by the U.S. both bilaterally to the Developing countries and through multilateral institutions was drastically cut off, from \$10.1 billion in 1988 to \$7.6 billion of 1989 (see table 4.1). This figure contrasted with the total amount of ODA bilaterally disbursed by the U.S. In 1989, the U.S. stepped up its disbursement, from \$6.7 billion to \$6.8 (see table 3.1) billion. It means that the drastic cut off only applied to the ODA extended through multilateral organizations. Since multilateral aid is regarded as freer from political strings

⁵⁰ Halldorsson, Jon (1989), "A Higher Profile for Indonesia," Southeast Asian Affairs 1989, Singapore: ISEAS, Boulder, Colorado: Westview Press, p.139.

or any non-developmental conditions pursued by the donor than aid disbursed bilaterally, this condition can also be interpreted to mean that the U.S. consciously used aid as a means for achieving its political objectives.

In term of concessionary aid, Japanese ODA to Indonesia has a grant element of an average 66.8 percent in the last ten years. In contrast, the total Japanese ODA has a grant element of 68.8 percent over the same period. It means that ODA provided to Indonesia is slightly less concessional than ODA extended to another country or multilateral organization. Compared with other DAC countries which extend aid to Indonesia, Japan is ranked the least in term of the concessionary element.

2. JAPAN'S INTERESTS IN SOUTHEAST ASIA

In general, the involvement of Japan in the Southeast Asian region is a reflection of Japanese motives in conducting foreign policy with the Third World countries. Japan regards the Developing countries as, *inter alia*, suppliers of raw materials or natural resources, a field for Japanese investment, a market for Japanese products, and directly or indirectly, the source or threat to Japan's security. These priorities or principles of Japanese foreign policy can also

be clearly seen in the way Japan concentrates its foreign aid allocation to the region.⁵¹

Some factors which encourage Japan to get involved closely in Southeast Asia through its aid can be explained as follows. First is historical colonial ties between Southeast Asia, including Indonesia, which is manifest in the practice of reparations payments as described above. Second, when expanding Japanese industries need market for their growing products, and ASEAN economies which grow relatively steady compared with the economies in the other parts of globe attracts Japanese business as their destinations. ASEAN countries as a unit are the important suppliers of natural resources or raw material such as oil, LNG, rubber, tropical timber, and tin. Third, Indonesia, Singapore, and Malaysia together control the Straits of Malacca through which passage of vessels to and from Japan. As a booklet on Philosophy of Economic Cooperation issued on April 1981 by MFA states:

"Indonesia, Singapore, Malaysia as guardians of the Straits of Malacca through which passes 85 percent of Japan's oil supply and 40 percent of its foreign trade. The Friendship of these nations is critical for Japan."⁵²

⁵¹ See Dore (1982), "Japan and the Third World: Coincidence or Divergence of Interests," in Cassen, *et. al.* (eds.), Rich Country Interests and Third World development, New York: St. Martin's Press, p.138-52.

⁵² Yasutomo (1986), Op Cit, p.31.

Fourth, For Japan, the ASEAN countries are hoped to provide a stabilization force for the unstable neighboring Indochina region.

3. INTERPRETATION OF JAPANESE AID INFLOWS TO INDONESIA

Japan's post war foreign policy is often described as "low-cost, low-risk foreign policy".⁵³ For many years it adopted a policy of *seikei bunri*⁵⁴, that is, to separate economics from politics. The principle of the policy is that Japan would concentrate on trade and other economic development activities and let the others afford costly military and political burdens.

As explained above, the emergence of Soeharto regime in Indonesia was welcomed by the Western countries. It can be said that the New Order government is a coalition of Japanese-trained generals⁵⁵ led by Soeharto and the U.S.-trained technocrats known collectively as "the Berkeley Mafia". Since then, large capital inflows from Japan has rushed in.

⁵³ Arase (1993), "Japanese Policy Toward Democracy and Human Rights in Asia," Asian Survey, Vol.XXXIII, No.10, October 1993, p.935.

⁵⁴ Ping (1990), Op Cit, p.163.

⁵⁵ Soeharto and his first generation of generals are the product of the so-called PETA (*Pembela Tanah Air*, literally meaning guards of father land), a military course conducted by Japanese colonial rule.

Indonesia has emerged as the largest recipient. Aid can be interpreted as the prize Japan should pay for the security of the supplies of natural resources or raw materials from Indonesia. By the end of 1960s, Indonesia was the third supplier of oil for Japan, after Iran and Saudi Arabia, accounting for 13 percent of Japan's total oil imports. The export value of Indonesia's oil to Japan accounted for \$318 million in 1970 and it doubled to \$648 million. In 1972, Indonesia, Malaysia, and Australia supplied more than 98 percent of the entire bauxite market in Japan. In 1973, Indonesia, Malaysia, and Thailand provided around 90 percent of total imported rubber.⁵⁶ Japan also is Indonesia's biggest customer for minerals. Almost all of Indonesia's mineral production such as tin, bauxite, copper ore, nickel, and aluminum is exported to Japan. Japan also imports around 300,00 tons of Indonesian coal a year in 1991.⁵⁷

According to one study, Japan prefers Indonesian oil to that from the Middle East because the latter has a higher sulfur content which exacerbates Japan's pollution problem.⁵⁸ Another factor is the closeness of distance between Japan and Indonesia which reduces the financial cost of shipping

⁵⁶ Hasegawa (1975), Op Cit, p.84.

⁵⁷ Marr (1993), Digging Deep, the Hidden Costs of Mining in Indonesia, London: Down to Earth, p.47.

⁵⁸ Caldwell (1974), "Oil Imperialism in Southeast Asia," in Selden, Mark (ed.), Remaking Asia: Essays on the American Uses of Power, New York: Pantheon Books, p.25.

compared with the cost of importing oil from the Middle East. Related to the issue of distance, shipping will also be relatively more assured.⁵⁹

With the first oil crisis of 1973, Japan increased its aid disbursement to Indonesia around 40 percent, from \$103 million in 1972 to \$143 million in 1973. In the following year this amount was raised another 50 percent, reaching \$221 million in 1974. This trend can be interpreted as a measure taken for securing oil supplies. The same step was also taken during the second oil crisis at the end of the 1970s. In 1980, Japan increased its ODA more than 50 percent over the preceding year, from \$227 million to \$350 million.

P.M. Kakuei Tanaka visited Indonesia in 15 and 16 January 1974 to protect the stability of Indonesia's oil supplies to Japan and to promote the development of supplies of LNG. Unfortunately, he was welcomed by a demonstration and rioting of Indonesian youths and students. They protested that Japanese foreign aid and investment were benefitting only a few and that the Japanese were exploiting the Indonesian economy. During the demonstration, usually called as *Malari* (Malapetaka Lima Belas Januari or "the disaster of January the fifteenth"), 11 youths were killed and more than a hundred

⁵⁹ For avoiding a route through increasingly hazardous and potentially hostile Strait Malacca, Japan once had an idea to construct a canal or pipeline across the narrowest part of the Kra Isthmus. See *Ibid*, pp.31-2.

injured. Some 1,000 vehicles were destroyed and 144 were burned or damaged.⁶⁰

The "January 15 Disaster" has been a valuable lesson for Japan. Japan began to reconsider its foreign aid policy. In the Summer 1975, P.M. Takeo Miki sent Saburo Okita, then chairman of OECF, to the ASEAN countries to survey the situation. Yet, instead of improving the quality of its ODA, Japan tended to increase its total amount disbursed. In 1976, Japan increased its ODA a little bit to Indonesia, from \$198 million in 1975 to \$201 million in 1976. At the same time, Japanese ODA in total decreased.

Aid to Indonesia has steadily declined from a high of \$350 million in 1980 to \$160 million in 1986. This trend can be explained by several factors. Japan at this period shifted its ODA to China. Japan was also under strong criticism from the international community on the way it concentrated its aid on Indonesia. As a consequence, Japan improved its ODA policy in 1983 in extending ODA to countries with the lowest per capita incomes.⁶¹ However, in practice Japan has not consistently applied this new policy. Japan is rather always

⁶⁰ Bresnan (1993), Managing Indonesia: The Modern Political Economy, New York: Columbia University Press, pp.135-47.

⁶¹ See Elsbree & Hoong (1985), "Japan and ASEAN," in Ozaki & Arnold (eds.), Japan's Foreign Relations: A Global Search for Economic Security, Boulder, London: Westview Press, pp.119-32.

inspired by pursuing or securing its economic or commercial interests in extending foreign aid.

Another factor which can explain why Japan disburses a significant amount of ODA is Indonesia's strategic position. As explained above, Indonesia, together with Singapore and Malaysia, controls the Strait Malacca through which vessels pass to and from Japan. It is hard for Japan to imagine a hostile Indonesia denying an international commercial passage through that Strait. Most of Japanese oil supplies and its foreign trade are routed via the Strait. In addition to the Malacca, Indonesia also has two strategic straits, namely the Sunda and Lombok, through which international shipping passes. They can be as ways of avoiding the crowded and busy Malacca strait.

In October 1988, the Indonesian government for the first time temporarily denied passage to all foreign vessels through the Sunda and Lombok Straits.⁶² Some analysts interpreted the move taken by the Indonesian government as directed towards Japan. By closing the Straits, which hit Japan's commercial interests hard, Indonesia wanted to pressure Tokyo to give more aid on more favorable terms. At the time, there was a signal from Tokyo that Japan would like to cut off the level

⁶² Pauker (1991), "Indonesia under Suharto: The Benefits of Aloofness," in Pipes, Daniel & Adam Garfinkle (eds.), Friendly Tyrants, An American Dilemma, New York: St. Martin's Press, p.379. In September 1989, again Indonesia takes a brief closure of the Lombok strait. See Vatikiotis (1993), "Indonesia's Foreign Policy in the 1990s," Contemporary Southeast Asia, Vol.XIV No.4, March, p.363.

of concessionary aid to Indonesia because Indonesia had been improving its economic growth rate.⁶³ In fact, in the consecutive three years, from 1987 to 1989, Japanese ODA disbursed to Indonesia was significantly increased. Over the period, Indonesia received \$707 million, \$985 million, and \$1,145 million respectively.

D. JAPANESE AID INFLOWS IN THE FUTURE

In the following years and those ahead, when Western aid donor countries are busy tying their aid disbursement to the practice of democracy, the record of human rights, and environmental preservation matters; we have not been able to see and are still hoping to see such enthusiasm emerge from the Japanese side. We have a reasonable hope that Japan might become the largest donor, surpassing the U.S. As a country which has enjoyed a great surplus against its trading partners, Japan should take a position as the leader among other donor countries by recycling more of its capital surpluses. When Japan becomes the leading donor society, the international community will demand that it not be as selfish as it has been so far, in comparison to other DAC members.

The end of the Cold War era also should have made Japanese reconsider its foreign aid practices. Redefining its

⁶³ Vatikiotis (1993), Ibid, p.363.

aid policy alone is not enough. The implementation of an improved policy is indeed expected. In fact, those who are eager to see the improvement of Japanese foreign aid practice should retain their optimism. Japan is seemingly not interested in the political nature of the countries to which it offers its aid. In the absence of any overt pressure from other nations, Japan is still less likely to tie its aid disbursement to Asian neighbors to such conditions adopted by any Western donors as human rights record, democracy, and other internal affairs of Asian recipients. This condition makes Japan attractive for Asian countries as an alternative source of capital for their economies.⁶⁴

It sometimes appears that whenever the external pressure is strong enough, Japan will "artificially" follow as a formality. Examples can be found in the practice of Japanese foreign aid towards China, Myanmar, and Indonesia itself. For the first two countries, Japan was the last donor country, after having overt pressure from other DAC countries, which postponed its aid disbursement to China as a protest of Chinese treatment of "tiananmen incident". Japan was the first donor countries which resumed its aid inflows, after

⁶⁴ Lincoln, Edward J. (1991), "Development in the Japanese Economy and Their Implication for the Asian Region," in Scalapino, Robert A. and Gennady I. Chufrin (eds.), Asia in the 1990s, American and Soviet Perspectives, Berkeley, California: Institute of East Asian Studies, University of California at Berkeley, p.189.

suspending aid only a short period⁶⁵ In September 1988, Japan froze its aid to Myanmar as a consequence of not recognizing the military regime of the State Law and Order Restoration Council (SLORC) which came to power through a *coup d'etat*. In February 1989, Tokyo recognized SLORC and resumed its aid disbursement to Myanmar.⁶⁶

In the case of Indonesia, Japan seems to be more reluctant to touch such sensitive areas in disbursing its aid. Some factors which explain this reluctance relate to the importance of Indonesia to Japan's economic interests. Japan has a great stake in the continuity of natural supplies: the security of sea-lanes upon which Japanese economic or commercial interests are dependent; and, of course, the endurance of political stability, all of which Japan has so far got from its good relations with Indonesia.

On November 12, 1991, the "Dili incident" in which some 50 unarmed demonstrators were killed, erupted. Some Western donors, i.e., the Netherlands, Canada, Denmark, and, to some extent the U.S., suspended its aid disbursement to Indonesia as a protest against the way the Indonesian government behaved in this event. Yet Japan announced the results of its

⁶⁵ See Zhou, Xiaoming (1991), "Japan's Official Development Assistance Program, Pressure to Expand," Asian Survey, Vol. XXXI No.4, April, pp.341-50.

⁶⁶ See, Seekins (1992), "Japan's Aid Relations with Military Regime in Burma, 1962-1991, The *Kokunaika* Process," Asian Survey, Vol. XXXII No.3, March, pp.246-62.

investigation that evidence of Indonesian official wrongdoing was "inconclusive". In late December 1991, there was overt pressure from Diet members against P.M. Miyazawa to link Japanese ODA to human rights. However, after an investigative commission created by Soeharto produced its report, the Japanese government asserted that there was "no need" to change its economic cooperation policies.⁶⁷

After Indonesia got assurance from Japan that it would continue to extend aid to Indonesia, Indonesia dared to refuse aid from the Netherlands and dismiss the Netherlands-led IGGI. The dismissal of IGGI allows for the following interpretation. Indonesia would have not rejected aid from the Netherlands if at the time Indonesia did not have assurance from Japan of a continuity in its aid inflows. It is so because the Netherlands' position as the chairman of the IGGI forum was so vital, regardless of its share, which was less than two percent of total aid channeled through IGGI. Refusing the Netherlands' aid meant practically the dismissal of IGGI. In terms of total aid provided to Indonesia, the Netherlands was "not so meaningful" compared with Japan which provided two-third of total bilateral aid received by Indonesia. The refusal of Dutch aid would not have a big impact on Indonesia.

In the eye of Western donors, the Japanese measure of guaranteeing the continuity of aid inflows to Indonesia was really controversial, even a "betrayal" of the principles of

⁶⁷ Arase (1993), Op_Cit, p.947.

protecting human rights and introducing democratic values which are vigorously campaigned for by them. Moreover it happened after the "Dili incident", in the post Cold War period. Even Japan has gone further by helping to organize a new forum called CGI which is officially chaired by the World Bank.

Another "controversial" political move taken by Japan is that Japan has signed the Bangkok Declaration on Human Rights in March 1993. The key points of the Declaration were that,

Developed countries should not tie aid to human rights, should respect the sovereign rights to manage human rights within their border, and should not promote human rights through "the imposition of incompatible values" on Asia.⁶⁸

It seems that Japan does not intend to use the principles of universal human rights, democratic values and other sensitive internal affairs of recipient countries in judging its aid allocation whenever its primary interests are at stake. In other words, the prospects for Japanese aid inflows to Indonesia in the years ahead will be slightly influenced by the universal principles taken by other Western donor countries. The trend of Japanese aid to Indonesia in the future will be more affected by the interaction between the level of its primary interest pursued in Indonesia and the opportunity or chance to achieve or fulfill those interests

⁶⁸ Arase (1993), *Ibid*, p.940.

offered by Indonesia. Aid is extended as *quid pro quo* for the opportunity offered to fulfil its primary or economic interests.

E. CONCLUSION

In contrast with the U.S., Japan does not intend to "calculate" political factors in disbursing its aid. Instead, the opportunities or chances to fulfil its economic interests are regarded as the determinant in providing aid. This is apparent when we look at its aid relations with Indonesia. Japan has been extending the largest amount of its total ODA to the New Order government of Indonesia since IGGI was created. Ever since 1974, a year after the first oil crisis, its ODA figure has surpassed that of the U.S. and since then Japan has been Indonesia's largest donor.

Some factors explain why Japan persists in disbursing its largest share to Indonesia. First, Japan is heavily dependent upon the supplies of natural resources for its economic survival. On the other side, Indonesia, which possesses abundantly natural resources, can fulfill the Japanese needs. Two oil crises, i.e. in 1973 and in 1979, have demonstrated that aid can be regarded as the high prize Japan should pay for the security of oil supplies. A year after each crisis, Japanese ODA was increased by 54 percent. Second,

geographically, Indonesia straddles two oceans and controls the strategic sea-lanes such as the Malacca, Sunda, and Lombok Straits. These sea-lanes, through which most of its natural resources inflows and its trade passage pass, have strategic importance for Japan. In 1988, for the first time Indonesia briefly closed of the Sunda and Lombok Straits. A year after this move, Indonesia got more Japanese ODA than a year before, reaching more than \$1 billion. Third, of course, the political stability of the Indonesian government keeps Japanese ODA flowing there. This factor is important, regardless of the nature of the regime, because for Japan in principle foreign aid cannot be separated from the other component of "economic cooperation" such as trade and investment. Indonesia's political stability and friendly political stance has made Indonesia the largest recipient of Japanese ODA since the New Order government came to power, except for the years 1983-86.

In the near future, Japan can be expected to be consistent in the way it allocates its ODA with the way it has done so far. It means that Japan is not willing to be "dictated" by the common principles vigorously promoted by the other Western donors, such as democracy, human rights, and environmental preservation matters. This tendency can be seen in the last three years. When the "Dili incident" erupted, some Western donors canceled their aid disbursement as a protest of official handling of the case. Yet Japan did not intend to follow its Western fellows and the Japanese

government did not even acknowledge that anything was wrong with Indonesia's official treatment of the problem. Japan took a further "controversial" political move by assuring two-thirds of total aid received by Indonesia and helping to organize a substitute for IGGI called CGI. In other words, the end of Cold War era has not seemed to change drastically Japanese aid practice, when and if its primary interests are at stake.

CONCLUSION

This study departs from the assumption that the practice of foreign aid relations which occurs bilaterally between donor and recipient countries is based upon the *quid pro quo* principle, mutual benefit. It means that there are expectations from the recipient country by the donor. Likewise, when the decision-makers in the recipient country consider seeking foreign aid, their preference to have aid disbursed from a certain country, along with their acceptance of a foreign aid offer, depends their political economic interests. Aid is used by the donor as a means of influence over the recipient country for the sake of the donor's benefit. A donor country will cancel its aid disbursement if its interests will not be fulfilled from the practice. The donor's power in this context lies in its aid disbursement. Conversely, the recipient country can also refuse aid when the practice is perceived as threatening to its sovereignty. The power of the recipient country rests in its political and economic importance as perceived by the donor. This strategic importance could depend on the recipient governments' political orientation or ideological stance, the stability of

its political condition, its country's location or natural resource base.

The study illustrates that the New Order government of Soeharto has enjoyed receiving aid inflows for more than one quarter of a century. In the first years, Soeharto's administration got a significant amount of aid from the Western countries, especially the U.S. Until 1971, Indonesia was the third largest recipient of the U.S. ODA, and accounted for 7.8 percent of total U.S. aid disbursed bilaterally, after India and Vietnam. At the time the U.S. was Indonesia's largest donor. Calculated from the total aid received by Indonesia through IGGI, the aid from the U.S. accounted for one-third. The New Order Government also was and is still the largest recipient of Japanese ODA. For the same period, Japan extended its ODA to Indonesia by more than 20 percent average of the total aid disbursed by Japan. Indonesia since then had been the largest recipient of Japanese ODA until 1983, when China temporarily replaced Indonesia's position and again since 1987 onward, Indonesia has enjoyed the lion's share of Japanese ODA. Japan has been Indonesia's largest donor since 1974 until now, replacing the American position.

As many studies reveal, aid inflows can be beneficial to the recipient country in financing its development when domestic savings raised are insufficient as illustrated by the "two-gap" model. Aid also can be harmful to the recipient countries, as both Liberal and Marxist critics argue. Instead

of aid being used for economic investment activities, aid is often wasted on non-development purposes and some poor countries are trapped in mounting foreign debt. The success of foreign aid depends on it being supported by effective management, and an environment conducive to sound management. The case of Indonesia confirms this proposition.

Generally, Indonesia's success in utilizing foreign aid cannot be separated from the condition of Indonesian political economy. Since Soeharto came to power, there is strict division of state management. Economic development is exclusively formulated and managed by economist-technocrats which are excluded from the political power arena. Meanwhile, to accommodate this economic development process, the government tightly controls or tames the political condition, which the military and the ruling party GOLKAR are entrusted to do.

Since its inception, the New Order government has undertaken the principle of "balanced budget" in which all foreign financing the government receives is treated as "foreign revenues". In the structure of the budget, all kinds of aid is allocated in the post "Development Revenues". Aid is utilized for economic investment activities. When we take a closer look at the composition of "Development expenditure", it is clear that four economic sectors are always given high priority by the government. Those sectors are Infrastructure, Agriculture and Irrigation, Human Resources, and Regional

Development. It means that most foreign aid money goes to finance the development of these sectors. The deliberate allocation of aid money in these sectors is based on political and economic considerations.

In the eye of the government, those sectors have strategic importance both economically and politically. Economically, especially in the first years of Soeharto's administration, the development of these sectors was prerequisite for achieving steady economic growth. Politically, concentration on developing these sectors was a strategic choice. The majority of Indonesian people live from agriculture and in rural areas. The social or political rebellions which were and could potentially be launched by either extreme Communists or Islamic fundamentalists always relied on the peasant community as their popular power base. Indonesia is a multi-ethnic society and this condition is still worsened by the social-economic imbalance between Java islands and the rest of Indonesian islands. The problem of economic gap is always the primary factor used by the extremists or fundamentalists to ignite a social or political revolution. In turn, this condition makes the government's political stability, or even the regime's legitimacy worse or in question. By developing these sectors, the government provide the majority of Indonesian people an equal chance to participate in production activity. As a consequence, the standard of living of the majority can be improved and

economic growth can be maintained at a steady level. From the political power stand point, foreign aid has been effectively directed by the government to prevent the potential secessionist movement or political unrest to explode. In conclusion, foreign aid has been utilized effectively by the government for developing or promoting economic sectors which are regarded as having strategic effects both economically and politically. The way the government directs or allocates aid monies has also to some extent explained the endurance of political stability and status quo Soeharto has so far enjoyed.

In the Cold War era, the U.S.'s foreign aid practice was based on political strategic considerations of containing Communist influence spreading to the Developing countries. The trend of its ODA concentration is in the area in which the intense ideological conflict between two Super Power occurs or is potentially to occur. In the first years after its Marshall Plan program, the U.S. concentrated its aid on the European continent because at the time the region was regarded as the main theater for bi-polar ideological conflict. Since the early 1950s, when the Korean War erupted, the U.S. began shifting its concentration in directing aid from Europe to Asia. U.S. aid inflows to this region reached an anticlimax when American constituent suffered from "aid fatigue" of the Vietnam war. However, the largest share of total American ODA still flowed to this continent. In the late 1970s, shortly

after the Camp David agreement was reached, the U.S. changed its direction from Asia to the Middle East region. Egypt and Israel, actually, have enjoyed the lion's share of U.S. ODA.

In the first years of Soeharto's coming to power, the U.S. extended its ODA to Indonesia in a significant amount, accounting for the third largest percentage after India and Vietnam. The U.S. was Indonesia's largest donor. Aid was regarded as a "reward" to the New Order government for being Western-oriented in conducting its foreign policy. Instead of yelling "go to hell with your aid" as Soekarno once did to the Kennedy administration, Soeharto relied on a group of American-trained economists, called the "Berkeley Mafia", for the economic development program. From the American point of view, the rise of the "Berkeley Mafia" as the main economic decision makers in Indonesia was an achievement of American foreign aid practice. In the political arena, the military disbanded the Communist party, arrests and execute its proponents, and eliminate its potential influence. The U.S.'s involvement in this political project is demonstrated by the U.S. embassy's providing the list of the PKI activists to the military and the "approval" of Indonesian military to seize East Timor before it would be a Communist country in the backyard of Indonesia. On the International scene, after Soeharto was in power, Indonesia was no longer hostile to the Western bloc. In fact, Indonesia broke its diplomatic ties with China and withdrew from the Communist bloc's orbit. In short,

foreign aid was used by the U.S. for keeping Indonesia in its orbit.

The prospect of the U.S.'s aid trend towards Indonesia is that it is rather demonstrably slowing down, instead of promising. This is not due to the steady growth level of the Indonesian economy, as a main factor influencing such a decreasing trend. The main reason is the demise of the Cold War period. In the post Cold War era, accompanied by the decline of U.S. economy, the U.S. is getting tight in disbursing its ODA and reconsiders its priority of aid direction. In the years ahead, the U.S. will tie its ODA with the practice of democratic values, Human Rights records, environmental preservation and impact, and other universal humanitarian concerns in the selection of the prospective recipient countries. On the contrary, Indonesian politics demonstrate opposite conditions to those regarded as ideal by the U.S. The "Dili incident", the "controversial" treatment of ex-PKI opponent prisoners, the relatively worse condition of Indonesian labor, and the development of economic infrastructure such as dams, roads, and electricity power which denies the demands of local communities whose properties are used for such projects are now The U.S.'s main concerns in extending its ODA to Indonesia. The U.S. government strongly criticizes these practices.

Unlike the U.S., Japan in disbursing its ODA is guided by its economic or commercial interests. For more than two

decades, its aid allocation has been concentrated in Asia and for that period of time Indonesia has enjoyed the lion's share of Japanese ODA, except from 1983-86 when its position as the largest recipient was temporarily replaced by China. As of 1974, a year after the first oil crisis erupted, Japan has been the largest donor for Indonesia.

This study reveals that Japan has been successfully extending its ODA to Indonesia for keeping the inflows of natural resource supplies from Indonesia and its commercial interests secure and stable. Aid is the cost Japan is willing to pay for the security of natural resources from Indonesia. Aid also is the effective means used by Japan to open the Indonesian market for its products. Another achievement is that Japan has skillfully used aid to keep open its sea-lanes for commercial passage from and to Japan.

We would argue that in the future the Japanese ODA inflows is not likely to be affected by political agendas such as democracy, human rights, and environmental preservation for which its Western donor fellows are at present vigorously pushing. The overall amount of Japanese ODA will be sustained if not increased in the near future. Japan's primary interests will continue to guide its aid direction.

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