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Sources and use of Indonesia's foreign debt from an Islamic economic perspective based on Siddiqi's theory

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ABSTRAK

Introduction

Foreign debt has been a significant factor influencing Indonesia's economic growth, both positively and negatively. Despite its role as a critical source of funding, mismanagement has led to dependency and economic challenges. Research on foreign debt from the perspective of Islamic economics remains limited, especially concerning its sources, utilization, and compliance with Islamic principles.

Objectives

This study aims to analyze the sources and uses of Indonesia's foreign debt from an Islamic economic perspective, utilizing M. Nejatullah Siddiqi's theory. It also seeks to assess how foreign debt aligns with Islamic principles and its implications for the country's economy.

Method

A qualitative research methodology was employed, focusing on a literature review of previous studies, policy documents, and secondary data related to Indonesia's foreign debt from 2009 to 2018.

Results

The study identifies that Indonesia's foreign debt is sourced through bilateral and multilateral loans and used primarily for infrastructure and public services. However, significant inefficiencies and interest-based practices conflict with Islamic principles, particularly the prohibition of riba (usury). Misallocation of funds and rising debt levels have further exacerbated economic disparities and dependency on external creditors.

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Implications
To reduce dependency on foreign debt and align financial practices with Islamic principles, policy recommendations include optimizing domestic resource management, implementing Sharia-compliant financing models, and improving accountability in public expenditure.

Originality/Novelty
This study provides a comprehensive analysis of Indonesia's foreign debt within the framework of Islamic economics, offering practical insights for policymakers to ensure sustainable and ethical economic practices while addressing the country's financial challenges.

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INTRODUCTION

Foreign debt has long been a critical element in the economic development strategies of many nations, particularly those with limited domestic capital to sustain growth (Bresser-Pereira & Nakano, 2003; Nölke et al., 2015; Shkolnyk & Koilo, 2018). For Indonesia, external borrowing has provided much-needed financial support to bridge fiscal deficits, finance infrastructure projects, and stimulate economic progress. However, this reliance on foreign loans has also exposed the country to various economic and political risks, such as dependency on external creditors, mismanagement of borrowed funds, and increasing fiscal deficits (Sunaryono et al., 2024; Triggs et al., 2019). The economic crisis of 1998 marked a turning point for Indonesia, amplifying the challenges of managing foreign debt amidst a depreciating currency and declining domestic revenue. The consequences of this crisis continue to resonate, underscoring the need for more sustainable and ethical approaches to external financing.

Despite its potential benefits, the practice of foreign borrowing often comes with significant drawbacks. Many studies have documented that foreign loans, particularly those obtained through interest-based mechanisms, exacerbate economic inequality, create fiscal imbalances, and foster dependency on international creditors (Bresser-Pereira & De Moraes Moreira, 2017; Helfstein, 2012; Queralt, 2022). According to Siddiqi's (1996) Islamic economic framework, these issues become even more critical when assessed against the principles of Shariah, which emphasize justice, transparency, and the prohibition of riba (usury). Recent literature highlights that while foreign debt can accelerate short-term development, its long-term implications are frequently detrimental, especially for countries like Indonesia, where the management and allocation of funds often fall short of optimal standards (Maharani & Widyastuti, 2024; Malini et al., 2022).

The primary research problem lies in understanding how Indonesia's foreign debt aligns—or fails to align—with Islamic economic principles. Conventional economic practices often prioritize interest-based borrowing due to its accessibility and flexibility, but this approach directly conflicts with Shariah's ethical guidelines (Mia, 2024; Nouman et al., 2021; Relano, 2023). The inability to comply with Islamic principles, combined with systemic inefficiencies in fund allocation, has led to persistent economic challenges for Indonesia. These include rising fiscal deficits, increasing social inequality, and a cyclical dependency on external borrowing to service existing debts. As such, the critical question arises: how can Indonesia reconcile the practical need for foreign financing with the ethical imperatives of Islamic economics?

A general solution to this problem often involves advocating for better fiscal management, improved accountability, and greater transparency in public spending. Moreover, countries are encouraged to explore alternative financing mechanisms that align with ethical and religious values. For Indonesia, this could mean transitioning from conventional debt instruments to Shariah-compliant financial models, such as sukuk (Islamic bonds) or other interest-free lending mechanisms. These alternatives not only adhere to Islamic principles but also offer opportunities to foster more sustainable and inclusive economic growth.

Specifically, recent studies emphasize the viability of integrating Islamic economic principles into foreign debt management. For example, previous studies suggest that adopting Shariah-compliant financing models could mitigate the adverse effects of interest-based loans while promoting economic justice (Afriyenis, 2016; Shaukat & Alhabshi, 2015; Tok & Yesuf, 2022). Similarly, Muhaimin (2012) highlights the potential of leveraging domestic resources and implementing Islamic financial instruments to reduce dependency on external creditors. These studies underscore the importance of aligning fiscal policies with ethical frameworks to achieve both economic sustainability and social equity.

A significant body of literature has explored the implications of foreign debt within the context of Islamic economics. Scholars such as Siddiqi (1996) and Kahf (1994) have extensively discussed the conditions under which borrowing is permissible under Shariah law. Their work emphasizes that foreign debt should only be pursued for essential purposes, such as national defense or addressing urgent fiscal needs, and must avoid riba, fraud, and exploitation. However, a notable gap remains in the application of these principles to contemporary economic policies, particularly in Indonesia. While prior research has provided valuable insights into the theoretical underpinnings of Islamic finance, there is a lack of empirical studies that evaluate the practical implementation of these principles in managing foreign debt.

This study seeks to fill that gap by analyzing Indonesia's foreign debt practices through the lens of Islamic economics, with a specific focus on Siddiqi's (1996) theoretical framework. By examining the sources and uses of foreign debt, the study aims to assess their compliance with Islamic principles and evaluate their impact on Indonesia's economic development. The research contributes to the existing literature by offering a comprehensive analysis that bridges theoretical insights with practical policy recommendations.

This study addresses a critical issue at the intersection of economics and ethics: how to manage foreign debt in a manner that is both sustainable and aligned with Islamic values. By providing a detailed examination of Indonesia's foreign debt practices, the study not only highlights the challenges inherent in conventional borrowing but also presents viable alternatives grounded in Islamic economic principles. This research is particularly relevant for policymakers, academics, and practitioners seeking to balance economic development with ethical considerations in an increasingly interconnected global economy.

LITERATURE REVIEW

Studies on the Sources and Uses of Foreign Debt from an Islamic Economic Perspective

The discourse on foreign debt has attracted significant scholarly attention due to its implications for economic development, fiscal sustainability, and social equity. In particular, the application of Islamic economic principles to foreign borrowing has emerged as a critical area of study, addressing the ethical and practical challenges posed by conventional debt mechanisms. Numerous studies have explored the sources and uses of foreign debt in the context of Islamic economics, providing theoretical and empirical insights into how these align—or fail to align—with Shariah principles (Chapra, 1992; Ismail & Dewi, 2015; W. M. Khan, 1989; Zubair & Muhammed-Mikaaeel, 2023).

Atmadja (2000) examined the evolution of Indonesia's foreign debt and its impact on national development. The study highlights that while foreign loans have historically bridged funding gaps, their allocation has often prioritized infrastructure projects over revenue-generating initiatives, leading to fiscal inefficiencies and a reliance on subsequent borrowing. Atmadja's analysis reveals a cyclical dependency on external creditors, exacerbated by the mismanagement of funds and a lack of focus on sustainable economic activities. Although this study does not explicitly address Islamic economic principles, it provides a foundational understanding of the systemic issues that undermine effective debt management.

Manoppo (2007) investigates the political economy of Indonesia's foreign debt, emphasizing the challenges posed by limited domestic revenue and the disproportionate allocation of borrowed funds. The study critiques the prioritization of urban development projects over equitable economic distribution, highlighting the systemic neglect of underdeveloped regions. While Manoppo's research is not explicitly framed within an Islamic context, its findings resonate with the principles of economic justice and transparency central to Islamic economics.

Muhaimin (2012) adopts a comparative approach, evaluating Indonesia's foreign debt management through both conventional and Islamic lenses. The study highlights the theoretical alignment of Shariah-compliant financial instruments with sustainable development goals, emphasizing their potential to reduce dependency on external creditors. By integrating Islamic macroeconomic policies into fiscal planning, Muhaimin argues that Indonesia can achieve greater financial autonomy and social equity.

Afriyenis (2016) offers a more targeted perspective, analyzing Indonesia's foreign debt from an Islamic economic framework. This study underscores the incompatibility of interest-based loans with Shariah, focusing on the adverse economic and social consequences of riba (usury). Afriyeni's advocates for the gradual reduction of external debt and the adoption of Shariah-compliant financing models to align fiscal practices with Islamic values. This research serves as a critical reference for policymakers seeking to reconcile economic growth with ethical considerations.

Andriansyah & Anto (2016) evaluate Indonesia's government spending during 2005–2013, using Siddiqi's Islamic framework to assess its alignment with Shariah principles. Their analysis reveals that while expenditures on education, social welfare, and infrastructure generally reflect Islamic teachings, inefficiencies and corruption compromise their effectiveness. The study highlights the potential of Islamic fiscal policies, such as zakat-based financing, to address social inequities and enhance fiscal responsibility. This work underscores the relevance of integrating Islamic economic values into Indonesia's fiscal planning to ensure equitable and sustainable development.

Atmaja et al. (2019) analyze Ad-Dawudi's classical contributions to public finance, particularly his categorization of state income into periodic (e.g., jizyah, kharaj) and non-periodic sources (e.g., zakat, ghanimah). The study highlights Ad-Dawudi's emphasis on ethical governance, balanced government spending, and social welfare, aligning these with Indonesia's fiscal policies. The findings suggest that although contemporary practices in Indonesia incorporate elements such as zakat and taxation, systemic challenges like corruption and inequitable resource distribution hinder full adherence to Islamic principles. This research provides a foundational understanding of how classical Islamic economics can inform modern fiscal policy.

Hamdi & Widiastuti (2021) explore the relevance of Islamic public finance principles, as proposed by Abu Ubaid and Ad-Dawudi, to Indonesia's fiscal context. They identify parallels between classical concepts such as zakat, kharaj, and fai' and modern revenue systems like taxes and state levies. However, the authors critique Indonesia's reliance on interest-based mechanisms, advocating for a transition to Shariah-compliant alternatives. This study serves as a significant contribution to understanding how Islamic economic principles can inform contemporary public finance management.

These studies collectively reveal a critical gap in the literature: while there is substantial theoretical work on the incompatibility of conventional debt mechanisms with Islamic principles, empirical analyses of Shariah-compliant alternatives remain limited. This gap underscores the need for research that not only critiques existing practices but also provides actionable frameworks for ethical debt management.

Islamic Economic Thought of M. Nejatullah Siddiqi

M. Nejatullah Siddiqi is widely regarded as a pioneer in contemporary Islamic economic thought, contributing extensively to the development of theoretical frameworks that reconcile economic practices with Shariah principles. His work addresses key issues such as public borrowing, interest prohibition, and the role of the state in ensuring economic justice (Parray, 2017; Ustaoğlu, 2023).

Siddiqi (1996) provides a comprehensive analysis of public borrowing within an Islamic framework, emphasizing that debt should only be undertaken for essential purposes, such as national defense or urgent public needs. He argues that such borrowing must avoid the four prohibited elements in Islam: riba, fraud, uncertainty (gharar), and exploitation (zulm). Siddiqi's work establishes a clear ethical boundary for public borrowing, advocating for transparency and accountability in debt management.

A recurring theme in Siddiqi's scholarship is the emphasis on aligning economic practices with moral and social objectives. He critiques the conventional economic focus on profit maximization, advocating instead for a balanced approach that considers the broader well-being of society. For example, Siddiqi's discussions on riba highlight its detrimental effects on economic justice and social equity, framing its prohibition as a cornerstone of Islamic economic policy (Wilson, 2014).

Siddiqi also addresses the structural and institutional dimensions of Islamic economics. He argues that the state has a proactive role in ensuring economic justice, particularly in the allocation of resources and the provision of public goods. This perspective aligns with the principle of amar ma'ruf nahi munkar (enjoining good and forbidding evil), extending its application to economic governance (Weill, 2014).

One of Siddiqi's significant contributions is his analysis of alternative financing mechanisms that adhere to Shariah principles. He emphasizes the potential of profit-sharing models, such as mudarabah and musharakah, as viable alternatives to interest-based loans. These models not only comply with Islamic ethics but also promote risk-sharing and equitable economic growth (Krichene, 2014).

The relevance of Siddiqi's work extends beyond theoretical discourse. His frameworks have practical implications for policymakers seeking to integrate Islamic principles into modern economic systems. By providing a detailed analysis of debt management, institutional reform, and resource allocation, Siddiqi offers a roadmap for ethical and sustainable economic practices (T. Khan, 2014).

Addressing Research Gaps

While Siddiqi's work has significantly advanced the theoretical foundations of Islamic economics, there is a need for empirical studies that evaluate the implementation of his principles in real-world contexts. For instance, the application of Shariah-compliant financing models to Indonesia's foreign debt remains underexplored. Existing literature tends to focus on the theoretical incompatibility of riba with Islamic principles, offering limited insights into the practical challenges and opportunities of transitioning to ethical alternatives.

This study seeks to bridge these gaps by applying Siddiqi's theoretical framework to analyze Indonesia's foreign debt practices. By examining the sources, utilization, and compliance of foreign debt with Islamic principles, the research aims to provide actionable insights for policymakers. Additionally, it addresses the broader question of how Islamic economic principles can inform sustainable and equitable development strategies in an increasingly interconnected global economy.

METHOD

Research Design

This study adopts a qualitative research methodology to analyze the sources and uses of Indonesia's foreign debt through the lens of Islamic economics. The research design is rooted in post-positivist philosophy, emphasizing the natural conditions and phenomena surrounding the research subject without external manipulation. The study relies primarily on secondary data sourced from government reports, scholarly articles, and existing literature. The qualitative approach allows for a detailed exploration of the issues related to foreign debt and their alignment with Islamic principles.

To enhance the reliability and comprehensiveness of the analysis, the study employs a literature review method as its primary data collection technique. This method provides a robust framework for synthesizing insights from existing research, policy documents, and statistical data related to Indonesia's foreign debt from 2009 to 2018. The use of triangulation ensures the credibility of the findings, combining data from various sources to construct a well-rounded understanding of the subject matter.

Research Focus

The focus of this study is on the sources and utilization of Indonesia's foreign debt, examined through the theoretical framework of M. Nejatullah Siddiqi's Islamic economic principles. The research specifically investigates whether the practices surrounding Indonesia's foreign borrowing comply with Shariah, particularly concerning the prohibition of riba (usury) and the ethical allocation of funds.

Data Collection Techniques

Data collection for this research is conducted through a comprehensive literature review, which involves the systematic identification, evaluation, and synthesis of relevant documents. Sources include government reports from the Ministry of Finance and Bank Indonesia, scholarly articles, books, statistical databases, and reputable online resources. As defined by Arikunto (2006), this method ensures the collection of accurate and comprehensive data by analyzing existing records such as transcripts, reports, journals, and other documentation.

The inclusion of official statistical reports, such as those provided by Bank Indonesia, ensures that the analysis is grounded in reliable and up-to-date information. The study also incorporates insights from previous scholarly works on

Indonesia's foreign debt and Islamic economic principles, allowing for a nuanced exploration of the research problem.

Data Types and Sources

The study relies exclusively on secondary data, which is collected indirectly through documentation. The secondary data used in this research includes:

- Official government publications, such as the Foreign Debt Statistics (*Statistik Utang Luar Negeri Indonesia* abbreviated SULNI in Bahasa Indonesia) from the Directorate General of Budget Financing and Risk Management (*Direktorat Jenderal Pengelolaan Pembiayaan dan Risiko* abbreviated DJPPR in Bahasa Indonesia) at the Ministry of Finance.
- Data from Bank Indonesia, detailing the classification and distribution of foreign debt by sector, purpose, and creditor.
- Scholarly articles and journal publications discussing the theoretical and practical dimensions of Islamic economics and foreign debt management.
- Books, websites, and other reputable sources that provide context and additional insights into the research focus.

These sources were chosen for their relevance and reliability in addressing the study's objectives.

Analytical Framework

The study employs an analytical framework grounded in M. Nejatullah Siddiqi's theory of Islamic economics. Siddiqi's framework emphasizes the ethical considerations surrounding public borrowing, particularly the prohibition of riba, the importance of transparency, and the alignment of economic practices with social and moral objectives. This theoretical lens is applied to evaluate Indonesia's foreign debt practices, focusing on:

1. The sources of foreign debt, including bilateral and multilateral loans, commercial loans, and Shariah-compliant financial instruments.
2. The utilization of borrowed funds, particularly in sectors such as infrastructure, public services, and economic development.
3. The compliance of these practices with Islamic principles, highlighting areas of alignment and deviation.

The analytical process involves three key steps, as outlined by Miles and Huberman:

1. Data Reduction: Organizing and simplifying the collected data to focus on the most relevant information related to the research objectives.
2. Data Presentation: Summarizing the findings in a clear and structured manner to facilitate interpretation and analysis.
3. Verification and Conclusion: Drawing conclusions based on the evidence presented and verifying the findings through triangulation and critical evaluation of the sources.

This approach ensures that the study provides a balanced and evidence-based analysis of Indonesia's foreign debt practices.

Research Validity and Reliability

To enhance the validity and reliability of the findings, the study incorporates several strategies:

- Triangulation: Data is collected from multiple sources to cross-verify the accuracy and consistency of the information.
- Purposive Sampling: Documents and data sources are selected based on their relevance to the research focus, ensuring that the analysis remains aligned with the study's objectives.
- Continuous Refinement: The research process involves iterative evaluation and refinement of the collected data to address any gaps or inconsistencies.

Scope and Limitations

The scope of this study is limited to the analysis of Indonesia's foreign debt from 2009 to 2018. While this timeframe provides a comprehensive overview of recent trends and practices, the reliance on secondary data may limit the ability to capture real-time policy changes or nuanced decision-making processes. Additionally, the study focuses on the macroeconomic implications of foreign debt, with limited attention to sector-specific outcomes or regional disparities.

Despite these limitations, the study offers valuable insights into the ethical and practical dimensions of foreign debt management within an Islamic economic framework. The findings contribute to the broader discourse on sustainable and ethical development strategies, providing actionable recommendations for policymakers and practitioners.

RESULTS

Development of Indonesia's Foreign Debt (2009–2018)

Indonesia's foreign debt has consistently increased over the years, reflecting the government's dependency on external financing to cover fiscal deficits and support national development initiatives. According to data from Bank Indonesia, the total foreign debt rose from $172.87 billion in 2009 to $377.36 billion in 2018, marking a significant 103.74% increase over this period. This upward trajectory underscores the persistent reliance on foreign loans to address budgetary shortfalls.

The debt comprises three main categories: government debt, central bank debt, and private sector debt. Government and central bank debt constituted the largest share, growing from $99.26 billion in 2009 to $186.27 billion in 2018. Within this category, government debt alone increased from $90.85 billion to $183.19 billion, while central bank debt showed a fluctuating trend, decreasing from $8.41 billion in 2009 to $3.07 billion in 2018. The private sector's foreign debt also demonstrated substantial growth, rising from $73.61 billion in 2009 to $191.08 billion in 2018, reflecting increased borrowing by financial and non-financial institutions.

Table 1

Development of Indonesia's Foreign Debt by Borrower Group, 2009-2018 (in Billion USD)

Borrower	2009	2010	2011	2012	2013
1. Government and Central Bank	99,265	118,624	118,642	126,119	123,548
1.1. Government	90,853	106,860	112,427	116,187	114,294
1.2. Bank Sentral	8,412	11,764	6,215	9,932	9,255
2. Private	73,606	83,789	106,732	126,245	142,561
2.1. Financial Institutions	9,530	17,957	24,570	30,730	32,378
2.1.1. Bank	64,075	14,382	18,466	23,018	24,431
2.1.2. Non-Bank Financial Institutions	3,066	3,575	6,103	7,713	7,947
2.2. Not a Financial Institution	61,009	65,833	82,162	95,515	110,183
Total	172,871	202,413	225,375	252,364	266,109
Borrower	2014	2015	2016	2017	2018
1. Government and Central Bank	129,735	129,736	142,608	158,283	180,622
1.1. Government	123,806	137,396	154,875	177,318	183,197
1.2. Bank Sentral	5, 930	5,212	3,408	3,304	3.023
2. Private	163,592	168,123	161,722	171,847	190,619
2.1. Financial Institutions	41,822	42,997	40,062	40,563	43,810
2.1.1. Bank	31,673	31,920	30,247	30,300	33,399
2.1.2. Non-Bank Financial Institutions	10,149	11,077	9,185	10,263	10,411
2.2. Not a Financial Institution	121,711	125,125	121,661	131,284	146,809
Total	293,328	310,730	320,006	352,469	376,839

Source: Direktorat Jenderal Pengelolaan Pembiayaan dan Risiko (2019a).

Sources of Indonesia’s Foreign Debt

The sources of Indonesia’s foreign debt are diverse, encompassing bilateral agreements, multilateral loans, and commercial borrowing. Bilateral loans are obtained through financial agreements with foreign governments, while multilateral loans come from international organizations such as the World Bank, the Asian Development Bank (ADB), and the Islamic Development Bank (IDB). Commercial borrowing involves the issuance of bonds and securities purchased by non-residents.

Bilateral creditors, including Japan, China, and Germany, have historically played a significant role in Indonesia's foreign debt landscape. For example, Japan remains one of the largest bilateral lenders, reflecting a longstanding economic partnership. Similarly, multilateral organizations provide substantial funding for large-scale infrastructure projects and poverty alleviation programs. Commercial loans, such as government bonds, have also gained prominence as a flexible financing instrument, particularly due to their ability to attract foreign investors.

Table 2

Foreign Debt by Creditor, 2009–2018 (in million USD)

Creditor	2009	2010	2011	2012	2013
1. Countries	111,650	118,272	140,477	153,555	163,122
United States	6,283	5,598	8,008	10,718	10,102
Australia	1,430	1,398	1,609	1,463	1,270
Austria	1,534	1,279	1,136	1,045	1,032
Netherlands	15,781	15,372	13,982	13,116	13,116
Belgium	464	621	746	969	1,024
Hong Kong	1,569	2,066	2,082	2,608	3,228
United Kingdom	3,312	3,096	2,931	3,091	3,641
Japan	3,218	40,473	43,774	40,062	32,826
Germany	35,401	3,604	3,658	3,388	3,225
South Korea	4,072	1,624	1,855	4,841	5,747
France	1,485	3,056	2,747	3,164	3,033
Singapore	3,183	24,724	38,497	42,288	49,830
Spain	22,338	500	469	445	383
Switzerland	533	968	1,133	1,193	1,586
China	983	2,488	3,701	5,060	6,158
Other Americas	2,351	2,078	2,697	3,422	3,875
Other Europe	1,098	2,422	3,298	4,541	4,416
Other Asia	2,571	2,989	4,014	4,821	6,238
Africa	556	642	666	766	737
Oceania	52	43	48	52	85
Syndicated Loans	3,436	3,236	3,182	5,908	8,883
2. International Organizations	24,970	26,667	27,033	27,413	27,126
ADB	11,233	11,636	11,436	10,895	10,895
IBRD	7,871	9,052	9,606	11,339	11,330
IDA	2,231	2,315	2,284	2,208	2,198
IDB	315	405	465	522	556
IFAD	77	81	119	130	145
IMF	3,093	3,050	3,008	3,053	3,050
NIB	64	51	45	34	32
EIB	86	77	68	59	49
Other International Organizations	-	-	-	-	-
3. Others	36,250	57,474	57,865	71,396	75,861
Total (1+2+3)	172,871	202,413	225,375	252,364	266,109
Creditor	2014	2015	2016	2017	2018
1. Countries	176,826	178,281	171,368	180,038	198,443
USA	11,663	10,267	10,586	12,630	21,056
Australia	1,328	1,394	1,547	1,272	1,177
Austria	812	619	523	472	403
Netherlands	11,705	11,110	8,890	10,707	8,667
Belgium	869	830	659	554	149
Hong Kong	6,725	7,886	13,203	13,276	15,035
UK	5,491	4,510	3,354	3,918	3,162

Japan	30,463	31,357	30,234	29,154	28,256
Germany	3,489	3,810	3,629	4,465	4,464
South Korea	6,232	6,150	6,558	6,438	6,438
France	3,033	3,260	3,556	3,322	3,322
Singapore	60,454	58,198	51,397	54,954	61,742
Spain	446	463	471	430	430
Switzerland	1,264	996	1,344	1,650	1,831
China	7,869	13,660	15,156	15,449	18,074
Other Americas	3,945	3,335	2,866	2,593	3,358
Other Europe	4,961	4,712	1,667	1,983	1,998
Other Asia	7,745	8,745	8,212	9,468	10,856
Africa	943	1,035	924	844	832
Oceania	58	55	31	31	35
Syndicated Loans	7,722	7,479	7,060	6,884	6,664
2. International Organizations	26,434	28,925	30,165	30,932	32,137
ADB	9,722	9,278	9,323	9,013	9,779
IBRD	12,187	14,380	15,812	16,563	16,753
IDA	1,880	1,677	1,474	1,390	1,194
IDB	643	701	643	909	1,055
IFAD	155	166	166	188	181
IMF	2,886	2,747	2,654	2,814	2,754
NIB	26	17	12	12	11
EIB	39	28	22	16	16
Other International Organizations	-	-	-	27	74
3. Others	90,068	52,104	118,473	141,498	146,775
Total (1+2+3)	293,328	310,730	320,006	352,469	377,355

Source: Direktorat Jenderal Pengelolaan Pembiayaan dan Risiko (2019b).

Notes: ADB: Asian Development Bank; IBRD: International Bank for Reconstruction and Development; IDA: International Development Association; IDB: Islamic Development Bank; IFAD: International Fund for Agricultural Development; IMF: International Monetary Fund; NIB: Nordic Investment Bank; and EIB: European Investment Bank.

Utilization of Foreign Debt

The utilization of foreign debt in Indonesia primarily revolves around financing economic development projects, repaying existing debt, and covering budget deficits. A substantial portion of these loans is allocated to infrastructure development, including transportation, energy, and public facilities. For instance, the government has used foreign debt to fund large-scale projects such as highways, ports, and power plants, which are expected to stimulate economic growth and improve public services.

Table 3

Government Foreign Debt Utilization by Sector, 2010–2018 (in million USD)

Sector	2010	2011	2012	2013	2014
Agriculture, Livestock, Forestry, and Fisheries	2,222	2,100	1,789	1,566	1,392

Mining and Quarrying	837	825	728	586	489
Manufacturing	2,007	1,887	1,543	1,151	885
Electricity, Gas, Steam, and Hot Water Supply	5,456	5,520	4,849	4,002	3,371
Water Supply, Waste Management, and Remediation	350	302	242	213	188
Construction	10,957	10,819	9,696	8,680	8,033
Wholesale and Retail Trade, Repairs	769	685	546	394	295
Transportation and Warehousing	760	943	884	923	822
Accommodation and Food Services	-	-	-	-	-
Information and Communication	1,451	1,365	1,198	1,007	798
Financial Services and Insurance	13,093	13,327	13,565	13,310	13,525
Real Estate	7	6	5	4	4
Business Services	18	17	16	16	13
Public Administration and Compulsory Social Security	41,578	47,630	55,789	60,024	74,921
Education	4,129	4,254	4,213	4,395	4,111
Health and Social Work	9,760	10,223	9,903	8,926	7,993
Other Services	13,464	12,525	11,222	9,097	6,967
Total	106,860	112,427	116,187	119,294	123,806

Sector	2015	2016	2017	2018
Agriculture, Livestock, Forestry, and Fisheries	8,872	9,827	10,678	10,747
Mining and Quarrying	522	506	507	504
Manufacturing	740	631	527	407
Electricity, Gas, Steam, and Hot Water Supply	3,501	3,657	4,012	4,050
Water Supply, Waste Management, and Remediation	2,966	2,616	3,418	4,012
Construction	19,780	22,593	30,353	31,332
Wholesale and Retail Trade, Repairs	229	177	127	81
Transportation and Warehousing	8,368	7,817	9,942	11,213
Accommodation and Food Services	-	-	-	-
Information and Communication	1,127	1,033	1,213	1,014
Financial Services and Insurance	20,467	24,710	24,130	26,959
Real Estate	3	2	3	2
Business Services	9	9	9	8
Public Administration and Compulsory Social Security	19,693	24,089	24,476	25,553
Education	20,684	23,289	27,851	28,700
Health and Social Work	23,744	28,727	35,541	33,934
Other Services	6,689	7,531	5,524	4,943
Total	137,396	154,875	177,318	183,197

Source: Direktorat Jenderal Pengelolaan Pembiayaan dan Risiko (2019b).

However, the effectiveness of this debt allocation has been questioned. Critics argue that a significant proportion of borrowed funds has been mismanaged or allocated to projects with limited revenue-generating potential. For example, infrastructure projects often face delays and cost overruns, reducing their anticipated economic benefits. Additionally, a considerable portion of the debt has been used to finance personnel expenses and administrative costs rather than productive investments. This misallocation undermines the debt's potential to contribute meaningfully to economic development.

Table 4

Private Foreign Debt Utilization by Sector, 2010–2018 (in million USD)

Sector	2010	2011	2012	2013	2014
Agriculture, Livestock, Forestry, and Fisheries	4,637	4,696	5,744	7,296	7,887
Mining and Quarrying	10,842	16,878	20,346	26,958	26,745
Manufacturing	19,471	22,646	25,637	28,984	32,461
Electricity, Gas, Steam, and Hot Water Supply	12,260	15,642	18,706	16,428	19,869
Water Supply, Waste Management, and Remediation	1	2	2	2	3
Construction	710	905	1,082	951	1,151
Wholesale and Retail Trade, Repairs	5,493	7,000	8,381	7,360	8,902
Transportation and Warehousing	3,295	4,199	5,028	4,415	5,340
Accommodation and Food Services	260	331	397	348	421
Information and Communication	4,437	5,654	6,769	5,945	7,190
Financial Services and Insurance	15,747	20,068	24,027	31,784	39,130
Real Estate	3,557	4,533	4,527	4,766	5,764
Business Services	1,158	1,476	1,767	1,552	1,877
Public Administration and Compulsory Social Security	16	21	25	26	25
Education	25	31	38	33	40
Health and Social Work	251	320	383	336	406
Other Services	1,630	2,077	2,487	2,379	2,580
Total	83,789	106,732	126,245	142,561	163,592

Sector	2015	2016	2017	2018
Agriculture, Livestock, Forestry, and Fisheries	8,298	7,003	6,366	5,995
Mining and Quarrying	25,390	23,254	23,078	29,102
Manufacturing	33,482	34,186	35,928	35,701
Electricity, Gas, Steam, and Hot Water Supply	19,567	20,034	24,533	30,951
Water Supply, Waste Management, and Remediation	3	3	3	11
Construction	1,115	1,249	1,251	1,848
Wholesale and Retail Trade, Repairs	9,381	8,564	9,494	9,974
Transportation and Warehousing	5,637	5,678	5,839	7,451
Accommodation and Food Services	408	416	530	534
Information and Communication	6,973	7,644	7,833	7,225
Financial Services and Insurance	42,203	39,311	40,912	45,646
Real Estate	6,282	5,341	6,081	5,887
Business Services	1,860	1,941	2,394	3,018
Public Administration and Compulsory Social Security	26	41	15	8
Education	64	13	15	14
Health and Social Work	403	439	480	475

Other Services	3,830	3,611	7,094	7,226
Total	168,123	161,722	171,847	191,080

Source: Direktorat Jenderal Pengelolaan Pembiayaan dan Risiko (2019b).

Islamic Economic Assessment of Foreign Debt

From an Islamic economic perspective, Indonesia's foreign debt practices present several challenges. The reliance on interest-based loans violates the principle of riba (usury), which is explicitly prohibited in the Quran. According to Siddiqi's (1996) framework, borrowing should align with ethical guidelines that promote economic justice and avoid exploitation. The use of interest-bearing debt mechanisms conflicts with these principles, raising concerns about the debt's compliance with Shariah.

Siddiqi (1996) emphasized that borrowing is permissible in Islam if it addresses genuine public needs, avoids exploitation (riba), and promotes equitable development. However, Indonesia's reliance on interest-based loans contravened the prohibition of riba in Islamic teachings. Such practices not only imposed financial burdens but also violated Islamic principles of mutual benefit and social justice. Siddiqi (1996) argued for debt to be directed toward essential services, such as poverty alleviation, education, and healthcare, while ensuring the absence of deceptive practices or unfair terms.

Additionally, the mismanagement of funds and the prioritization of non-productive expenditures contravene the Islamic emphasis on accountability and transparency. Shariah requires that public borrowing serve the collective welfare and focus on projects that deliver tangible benefits to society. The current practices, which often favor short-term political gains over long-term economic sustainability, fail to meet these ethical standards.

Economic Implications of Rising Foreign Debt

The persistent increase in foreign debt has significant economic implications for Indonesia. One of the most pressing concerns is the growing fiscal burden associated with debt repayment. Interest payments and principal repayments consume a substantial portion of the state budget, diverting resources away from critical sectors such as education and healthcare. This situation creates a cycle of dependency, where new loans are required to service existing debts, exacerbating the financial strain on the economy.

Moreover, the reliance on foreign debt exposes Indonesia to external risks, such as currency fluctuations and changes in global interest rates. For example, the depreciation of the Indonesian rupiah against the US dollar during the 1998 economic crisis sharply increased the cost of foreign debt repayment. Such vulnerabilities highlight the need for more resilient and self-reliant financing strategies.

Another critical issue is the impact of foreign debt on economic inequality. While urban areas benefit from infrastructure projects funded by foreign loans, rural and underdeveloped regions often receive limited attention. This uneven distribution of resources perpetuates regional disparities, undermining the Islamic principle of equitable development.

Alignment with Islamic Principles

Despite the challenges, there are opportunities to align Indonesia's foreign debt practices with Islamic economic principles. Shariah-compliant financing instruments, such as sukuk (Islamic bonds), offer viable alternatives to interest-based loans. Sukuk allows the government to raise funds without violating the prohibition of riba, as they are structured around profit-sharing or asset-based mechanisms. Several countries, including Malaysia and Saudi Arabia, have successfully implemented sukuk to finance public projects, demonstrating its potential as an ethical and sustainable financing option.

In addition to adopting Shariah-compliant instruments, Indonesia could improve its debt management practices by enhancing transparency and accountability. This involves ensuring that borrowed funds are allocated to projects with clear economic and social benefits, minimizing waste and inefficiency. By aligning borrowing practices with Islamic principles, Indonesia can address the ethical concerns associated with foreign debt while fostering sustainable development.

DISCUSSION

The Role of Foreign Debt in Indonesia's Economic Development

Foreign debt has played a pivotal role in Indonesia's economic development, particularly in addressing budget deficits and financing large-scale infrastructure projects. However, the reliance on external loans has raised critical concerns about sustainability and ethical practices. While these funds have provided short-term solutions to fiscal constraints, their long-term implications reveal systemic inefficiencies and mismanagement. According to previous studies, the allocation of foreign debt has often prioritized infrastructure over revenue-generating initiatives, resulting in limited economic returns and an ongoing dependency on borrowing (Atmadja, 2000; Hassan et al., 2022; Mubin, 2019; Ramadani et al., 2023). This trend highlights a persistent challenge in optimizing the use of borrowed funds for sustainable development.

From an Islamic economic perspective, the ethical considerations surrounding foreign debt are particularly significant. The principles of Shariah emphasize justice, transparency, and accountability in financial transactions (Bhatti & Bhatti, 2010; Laldin, 2010; Nienhaus, 2011), all of which are crucial for ensuring that public borrowing serves the collective welfare. However, Indonesia's reliance on interest-based loans conflicts with these principles, raising questions about the ethical alignment of its debt management practices.

Mismanagement and Inefficiencies in Debt Utilization

One of the primary issues identified in this study is the mismanagement of foreign debt. A significant portion of borrowed funds has been allocated to administrative expenses and personnel costs rather than productive investments. For instance, as noted by previous studies, funds intended for infrastructure projects are often subject to delays and cost overruns (D. Kurniawan et al., 2022; Manoppo, 2007; Rauzana et al., 2022; Susanti, 2020), diminishing their potential economic benefits. This misallocation not only undermines the effectiveness of foreign debt but also exacerbates economic disparities by prioritizing urban development over rural needs.

Additionally, the lack of transparency and accountability in debt management has compounded these inefficiencies (Harun et al., 2019; Trimarstuti, 2019). The absence of clear frameworks for evaluating the impact of foreign debt on national development has led to suboptimal decision-making. Siddiqi's (1996) framework underscores the importance of aligning public borrowing with ethical guidelines that promote accountability and equitable resource distribution. However, the current practices in Indonesia fall short of these standards, highlighting the need for systemic reforms in debt governance.

The Ethical Implications of Interest-Based Borrowing

Interest-based borrowing, or riba, is explicitly prohibited in Islamic economics due to its exploitative nature and potential to perpetuate economic inequalities (Abedifar, 2019; Rab & Anjum, 2011; Sifat & Mohamad, 2018). The reliance on riba-based loans poses a significant ethical dilemma for Indonesia, as it contravenes the principles of Shariah. According to previous studies, the use of interest-bearing debt mechanisms not only violates Islamic ethics but also imposes a heavy fiscal burden on the government, diverting resources away from critical sectors such as education and healthcare (Afriyenis, 2016; Diallo & Gundogdu, 2021; Kasanah & Ryandono, 2022).

The negative economic implications of riba are evident in the growing debt repayment obligations, which consume a substantial portion of the state budget. This situation creates a cycle of dependency, where new loans are required to service existing debts, perpetuating financial instability. Siddiqi (1996) emphasizes the importance of adopting alternative financing models that align with Islamic principles, such as profit-sharing arrangements or Shariah-compliant bonds. These alternatives offer viable solutions to the ethical challenges posed by conventional debt mechanisms.

Potential of Shariah-Compliant Financing Models

Shariah-compliant financing instruments, such as sukuk (Islamic bonds), present a promising alternative to interest-based loans. Unlike conventional debt mechanisms, sukuk are structured around asset-backed or profit-sharing arrangements, ensuring compliance with Islamic principles (Abubakar et al., 2023; Raghibi & Oubdi, 2021; Saleh & Alswaidan, 2024; Selim et al., 2023). Countries like Malaysia (Abd Majid et al., 2020; Hasan et al., 2022; Liu & Lai, 2021; Mohd. Zain et al., 2021) and Saudi Arabia (Al Madani et al., 2020; Althyabi, 2023) have successfully implemented sukuk to finance public projects, demonstrating its potential as an ethical and sustainable financing option.

In the context of Indonesia, adopting sukuk could address several challenges associated with foreign debt. First, it would eliminate the reliance on riba-based loans, aligning the country's financial practices with Islamic values (T. Kurniawan & Ab Rahman, 2020; Pratama et al., 2020). Second, sukuk promote greater transparency and accountability (Supriyadi et al., 2023; Surachman et al., 2023), as they require detailed documentation of the underlying assets and the expected returns. This ensures that funds are allocated to productive investments that deliver tangible economic and social benefits.

Additionally, sukuk can attract a broader investor base, including those seeking ethical investment opportunities (Hassan et al., 2022; Uluyol, 2023). By leveraging its position as the world's largest Muslim-majority country, Indonesia can tap into the growing global market for Islamic finance, reducing its dependency on conventional debt instruments.

Addressing Economic Inequality Through Ethical Debt Management

One of the fundamental objectives of Islamic economics is to promote economic justice and reduce inequalities. However, Indonesia's current debt practices have often prioritized urban development at the expense of rural and underdeveloped regions. This uneven allocation of resources perpetuates regional disparities, undermining the principles of equitable development.

To address this issue, debt management practices must prioritize projects that promote inclusive growth and improve the livelihoods of marginalized communities. This includes investing in rural infrastructure, education, and healthcare, which have a direct impact on poverty alleviation and social mobility. By aligning borrowing practices with the principles of economic justice, Indonesia can ensure that foreign debt contributes to sustainable and equitable development.

Risks and Challenges in Transitioning to Ethical Financing

While the adoption of Shariah-compliant financing models offers significant benefits, it also presents certain challenges. One of the primary obstacles is the lack of familiarity with Islamic financial instruments among policymakers and financial institutions. This necessitates capacity-building initiatives and awareness campaigns to ensure a smooth transition.

Another challenge is the potential resistance from international creditors, who may be less willing to accommodate Shariah-compliant arrangements. To overcome this, Indonesia must actively engage with global Islamic finance networks and foster collaborations with countries that have successfully implemented such models. Additionally, regulatory frameworks must be strengthened to support the integration of Islamic finance into the national economy.

Policy Recommendations for Sustainable Debt Management

To address the challenges associated with foreign debt, several policy recommendations emerge from this study:

1. Adopt Shariah-Compliant Financing Instruments: Transitioning to sukuk and other Islamic financial instruments can reduce the reliance on riba-based loans and align debt practices with Islamic principles.
2. Enhance Transparency and Accountability: Establishing clear frameworks for evaluating the impact of foreign debt on national development can improve decision-making and reduce inefficiencies.

3. Prioritize Inclusive Development: Allocating borrowed funds to projects that promote equitable growth, such as rural infrastructure and public services, can address regional disparities and foster social equity.
4. Strengthen Institutional Capacity: Investing in capacity-building initiatives for policymakers and financial institutions can facilitate the adoption of ethical financing models.
5. Leverage Global Islamic Finance Networks: Engaging with international Islamic finance organizations can provide access to ethical investment opportunities and technical expertise.

CONCLUSION

Indonesia's reliance on external debt has been a long-standing issue, intensified since the 1998 economic crisis, which disrupted various sectors and caused significant fiscal challenges. The government's decision to borrow from foreign institutions and governments addressed immediate financial needs but created a dependency on external funding. Despite the influx of these loans, their impact on national revenue generation has been minimal, leaving the country with a mounting debt burden.

The interest-based nature of external loans has compounded Indonesia's debt challenges, leading to unsustainable financial obligations. This system not only contravenes Islamic principles, which prohibit riba but also hampers economic progress. The consistent increase in external debt highlights structural inefficiencies and the lack of self-reliant economic strategies to address fiscal deficits without resorting to borrowing.

In conclusion, while external debt has played a role in addressing short-term financial gaps, its long-term effects have been detrimental. There is an urgent need for Indonesia to adopt a more sustainable financial model that prioritizes revenue generation, reduces dependency on loans, and aligns with ethical financial principles.

Limitation of the Study

This study focuses on Indonesia's external debt, emphasizing its historical context, economic implications, and compliance with Islamic principles. While it provides a comprehensive overview, the research relies heavily on secondary data, which may limit the scope for nuanced insights into the real-time policy and economic decisions of the government.

Additionally, the study primarily evaluates the macroeconomic impacts of external debt and does not delve into sector-specific outcomes or the granular allocation of borrowed funds. Understanding how loans have affected specific industries or public services could provide more actionable insights for policymakers and stakeholders.

The lack of comparative analysis with other developing countries also limits the study's generalizability. While Indonesia’s case is unique in its socio-economic and political context, exploring parallels with other nations could highlight broader lessons or strategies to address similar challenges in debt management.

Recommendations for Future Research

Future research should explore alternative financial models that Indonesia could adopt to reduce dependency on external debt while fostering economic growth. Particular attention should be paid to implementing interest-free financing methods, such as sukuk or other Islamic financial instruments, that align with the country's values and offer sustainable solutions.

Additionally, studies should examine the sector-specific impact of external debt, focusing on industries like infrastructure, education, and healthcare, to evaluate whether borrowing has delivered tangible benefits. This would involve assessing whether the outcomes justify the costs, especially given the high interest rates associated with these loans.

Lastly, comparative studies analyzing external debt strategies of other developing countries could offer valuable insights for Indonesia. By exploring successful debt management practices globally, future research can propose tailored strategies that address Indonesia's unique fiscal challenges while ensuring ethical compliance and long-term sustainability.

Author Contributions

Conceptualization	N.A.T.A.S. & Y.A.	Resources	Y.A.
Data curation	N.A.T.A.S. & Y.A.	Software	N.A.T.A.S. & Y.A.
Formal analysis	N.A.T.A.S., Y.A., & V.N.	Supervision	Y.A.
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Investigation	N.A.T.A.S. & Y.A.	Visualization	N.A.T.A.S. & Y.A.
Methodology	N.A.T.A.S. & Y.A.	Writing – original draft	N.A.T.A.S., Y.A., & V.N.
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Informed Consent Statement

Informed consent was not required for this study.

Data Availability Statement

The data presented in this study are available on request from the corresponding author.

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Conflicts of Interest

The authors declare no conflicts of interest.

Declaration of Generative AI and AI-Assisted Technologies in the Writing Process

During the preparation of this work the authors used ChatGPT, DeepL, Grammarly, and PaperPal in order to translate from Bahasa Indonesia into American English, and to improve clarity of the language and readability of the article. After using these tools, the authors reviewed and edited the content as needed and take full responsibility for the content of the published article.

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