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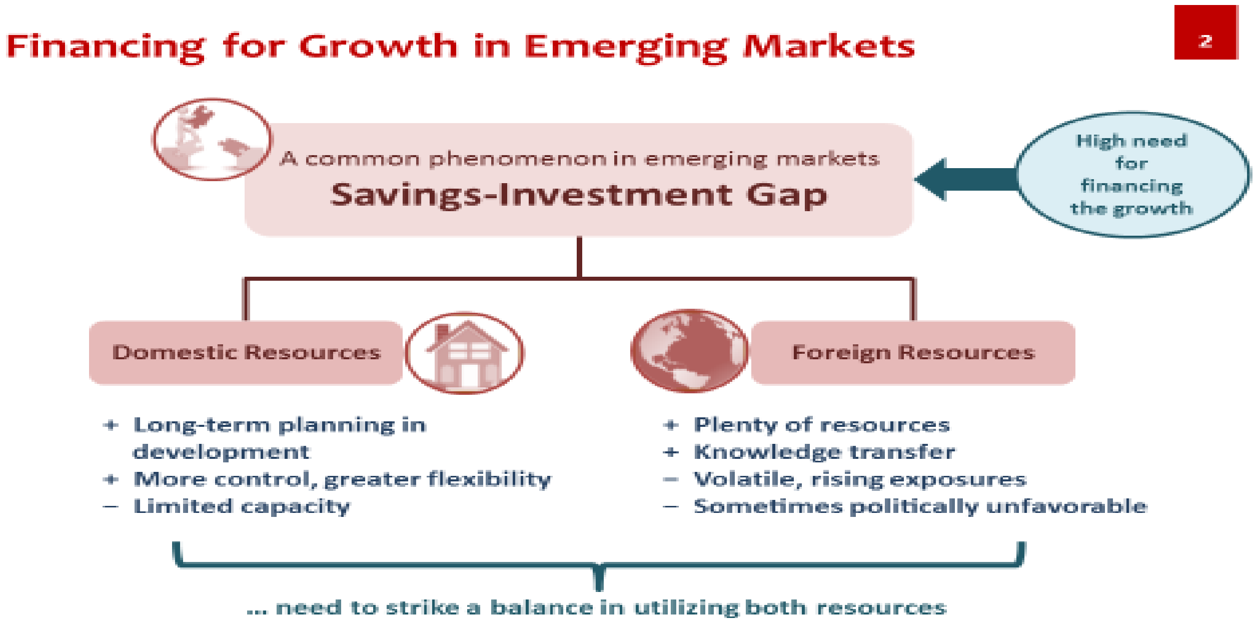
CHAIRMAN OF THE BOARD OF COMMISSIONERS
INDONESIA FINANCIAL SERVICES AUTHORITY (OJK)

"Mobilizing Domestic Resources Through Financial Sector: Unlocking Opportunities For Growth"

Joint IMF-BI Conference
Jakarta, 2 September 2015



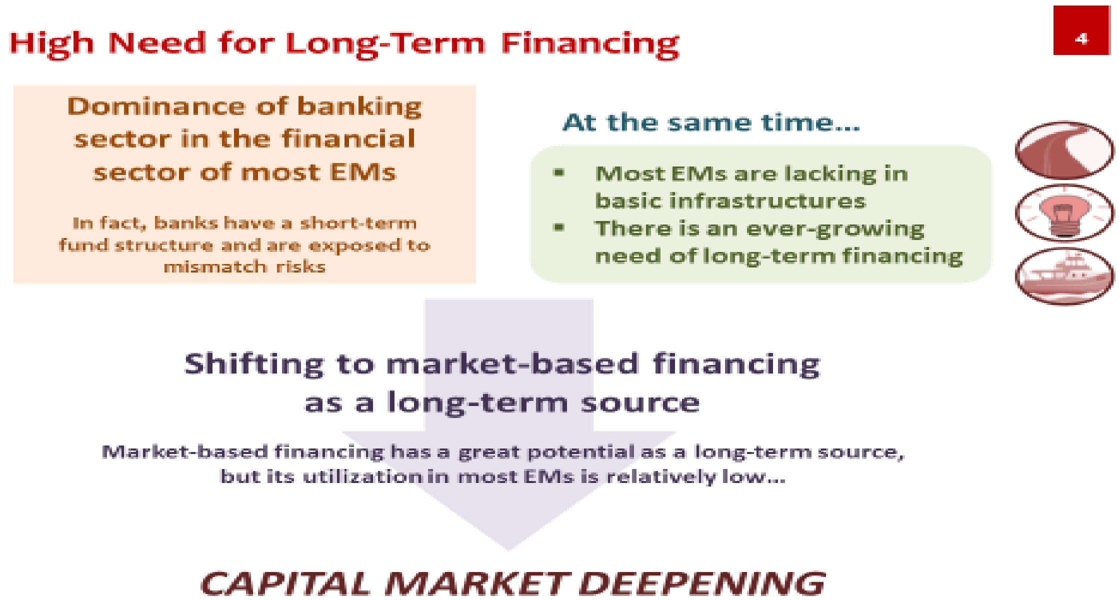
Slide 2: Financing for Growth in Emerging Markets

- There is a common phenomenon found in emerging markets (EMs), namely the gap between savings and investments. This phenomenon is understandable, since such economies usually need more investments in their economic development process. In overcoming the savings-investment gap, EMs may utilize various sources to finance their growth. Basically, there are two types of resources, namely domestic and foreign ones.
- I acknowledge that **domestic resources** mobilization will play an important role in financing the gap. It even becomes one of the initiatives in the Sustainable Development Goals.
- The use of domestic resources has its own advantages and disadvantages. It encourages long-term planning in development, and also provides more control and flexibility. However, as experienced by many EMs, the standalone domestic resources cannot fulfill the need for growth financing, leading to the utilization of foreign resources.
- Indeed, there are plenty of **foreign resources** choices, among others foreign debt, foreign direct investments, portfolio investments, and official development assistance. The utilization of foreign resources also offers some advantages like transfer of knowledge. However, utilizing foreign resources is exposed to the risks of volatility and rising exposures, and may be politically unfavorable.
- Nevertheless, we are aware that in many cases, foreign resources are still needed, and its utilization should be in line with national interests. In short, for emerging markets, there is a need to strike a balance in utilizing both types of resources.

Slide 3: Development Funding Needs

- As part of domestic resources, financial sector plays an important role to fulfill the needs for development financing. If we look into historical data on funding provision by financial sector, the annual average of funding provision by the financial sector (during the period 2010-2014) was USD 43.6 billion. The banking sector accounts for 75% of total funding provided by the financial sector.

- In our medium-term development, financial sector is expected to play an even greater role in providing funding for development. As targeted by the 2015-2019 National Medium-Term Development Plan, financial sector is expected to provide 30% of total funding needs (USD 0.57 trillion out of USD 1.9 trillion). Of course, this is a very challenging target and there is a high need to mobilize all possible resources.



Slide 4: High Need for Long-Term Financing

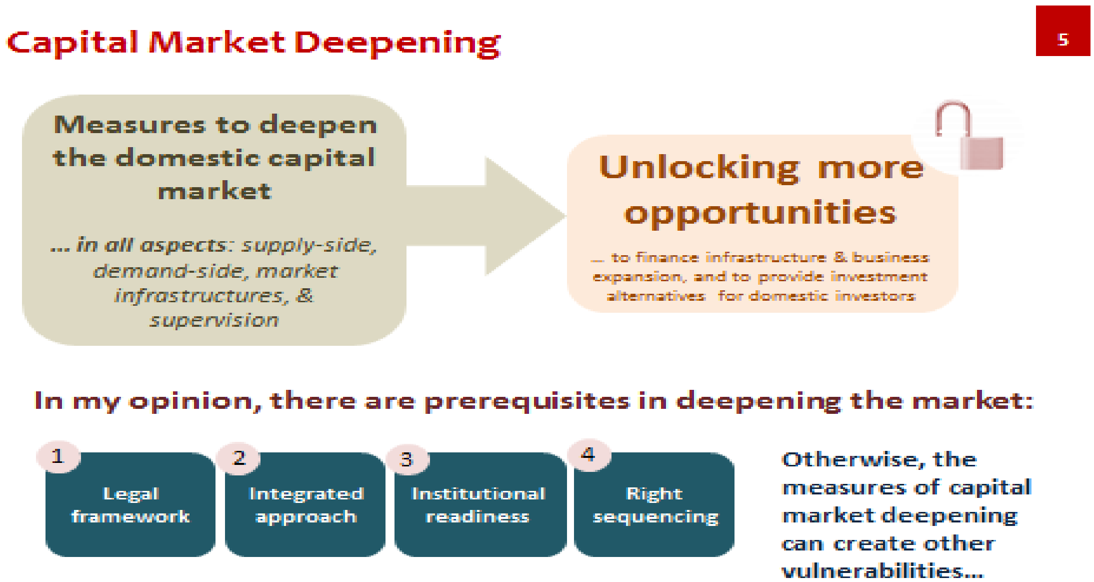
- Since domestic resources from the public sector (i.e. taxation) hardly cover the need of development financing, the private sector hence plays a vital role. In this case, financial sector appears to be one of the important sources.

- In EMs, the banking sector is usually the dominant player in the financial sector. This is also the case of Indonesia, where our banking sector accounts for 74% of the financial sector's total assets. However, we are aware that banks naturally have a short-term fund structure and are exposed to mismatch risks. At the same time, most EMs are lacking in basic infrastructures, and there is an ever-growing need of long-term financing.

- Thus, we have to seek alternative sources. Market-based financing has a great potential as a long-term source. However, in most EMs, we could see that the utilization of the capital market is relatively low.

- Shifting to the market-based financing as a long-term source should be in our top priority. Of course, it does not mean that the role of the banking sector is to be reduced. We just would like to see the capital market to play an increasingly significant role to finance our economic growth.

- We need to expand our capital market through market deepening initiatives.



Slide 5: Capital Market Deepening

- I believe measures to deepen the domestic capital market should cover all aspects: supply-side, demand-side, market infrastructure, and supervision.

- The supply-side should be enhanced through—among others—encouraging more firms to accumulate funds through the capital market and providing diverse instruments for investments. Meanwhile, the demand-side should also be strengthened through enhancing the role of institutional investors (e.g. insurance companies & pension funds), expanding distribution channels for market products as well as promoting the awareness and financial literacy of the society.

- When such measures are conducted effectively, we expect that a lot of opportunities will be unlocked. Thereby, the capital market will be increasingly important to finance infrastructure projects undertaken by either the private sector or the Government. In addition, the capital market would be more optimal in financing expansion of businesses, and provide good investment alternatives for domestic investors.

- In my opinion, there are a number of prerequisites if we would like to deepen the capital market. Those prerequisites are, among others: (1) institutional readiness, (2) integrated approach, (3) legal framework, and (4) which is one of the weaknesses in EMs, i.e. **right sequencing** of capital market deepening. Without the fulfillment of such prerequisites, the measures of capital market deepening can create other vulnerabilities.

Legal Framework

- A more sophisticated financial products or engeenering has to be accompanied by sufficient legal framework. It is a common phenomenon in EMs that there is no sufficient framework to support product development, as well as consumer protection and legal enforcement.

- Indeed, regulations will not be effective unless there is an adequate framework protecting the rights of investors and creditors.

Integrated Approach

- In undertaking measures of capital market deepening, we should put concerns on supply-side, demand-side, market infrastructure, and supervision—where all of these aspects should be conducted simultaneously. For example, innovations of new products should suit investors' characteristics, infrastructure readiness, and supervisory capacity.

- Finally, financial deepening is directed to ensure the availability of market liquidity and products, at any time and a fair price.

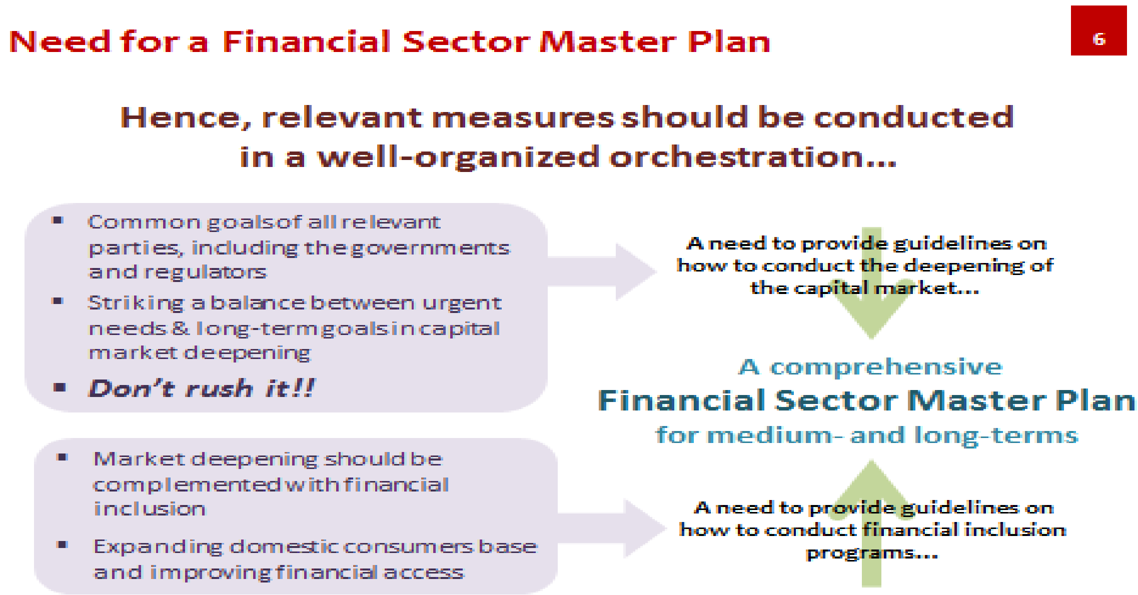
Institutional Readiness

- Another important factor is institutional readiness, for example in terms of clarity of function and authority, as well as inter-agency coordination. It is clear that a number of issues can only be solved through coordination between two or more institutions. For example, product development should be complemented by supporting taxation environment, etc.

Right Sequencing

- In market deepening, the sequence of development should be in line with product complexity, infrastructure, and supervision. For example, product development should not be rushed when the infrastructure is not ready yet, etc.

- We can see, many EMs are facing increasing pressures when they are exposed to recent shocks. Therefore, sequencing of the deepening initiatives should be performed in a "right" sequencing, depending on the fulfillment of the prerequisites.



Slide 6: Need for a Financial Sector Master Plan

- Measures to deepen the capital market need to be conducted in a well-organized orchestration. Such measures should take into account the common goals of all relevant parties, including the Government and regulatory agencies. Another important point is that we should strike a balance between urgent needs and long-term goals. And also, ***we should not rush it***!! Accelerating the deepening measures does ***not*** mean that we should rush and ignore important points along the process.

- Furthermore, market deepening should be complemented with financial inclusion. In EMs, financial inclusion is as important as financial deepening itself, through the expansion of domestic consumers base and the improvement of financial access. These two initiatives will in turn support financial system stability.

- To achieve the desired goals, then we need a guideline on how to conduct capital market deepening, how to conduct financial inclusion programs, and so forth. Here, we underline the importance of a comprehensive Financial Sector Master Plan for the medium- and long-terms.

- Within the context of Indonesia's financial sector, OJK is now in process of formulating a Financial Sector Master Plan 2015-2019, which will provide guidelines to develop our financial sector in the medium-term. The Master Plan has taken into considerations the National Medium-Term Development Plan set by the Government.

Slide 7: Three Directions for Indonesia's Financial Sector

- OJK has clearly set out 3 directions to develop Indonesia's financial sector in the medium-term. From each direction, key priorities and programs are derived. A comprehensive "Indonesia's Financial Sector Masterplan" is scheduled to be launched in Semester 2-2015.

- There are three main directions in developing our financial sector, namely:

  - **Enhancing financial sector's role in fostering domestic growth**. In ongoing efforts to achieve a robust and sustainable economic growth, the domestic financial sector is directed to play a more vital role in terms of catalyzing national economic activities.

  - **Strengthening financial sector's resilience to maintain financial system stability**. To support the sustainability of economic development, financial stability plays an important role. To that end, financial sector must maintain its resilience to confront possible shocks that could emerge from the domestic or external environments.

  - **Enhancing financial sector's role in improving financial inclusion and promoting equality**. Financial sector has the opportunity to play an increasingly significant role in overcoming inequality that may arise. Initiatives undertaken by OJK include promoting financial inclusion and catalyzing local economy.

Slide 8: Three Directions for Indonesia's Financial Sector

- In **enhancing financial sector's role to foster growth**, programs and initiatives undertaken by OJK are focused on the enhancement of the role of the financial sector in development financing, as well as in promoting competitiveness and economic growth.

- To **strengthen financial sector's resilience to maintain financial stability**, OJK put concerns on the strengthening of integrated supervision. We also conduct measures and initiatives in terms of enhancing regulations on information disclosure, corporate governance, and market participants' behavior; as well as promoting measures of capital market deepening as previously explained.

- In order for the financial sector **to contribute to improving the prosperity of Indonesians**, OJK offers some initiatives and breakthroughs. We improve access to financial services by Indonesians of all social classes. Financial sector is also directed to enhance its role as a catalyst for the local economy. As mentioned earlier, financial education and inclusion will also be continuously improved, unlocking opportunities for growth by promoting wider participation of the public through utilization of financial services.

Concluding Remarks

- In conclusion, for me, mobilizing domestic resources is indeed important. But, we are aware that the standalone domestic resources will be never enough to finance our growth. We still need a balance in utilizing both domestic and foreign resources, and in doing so, market deepening and financial inclusion initiatives should become the answer and be conducted simultaneously.

- A comprehensive Master Plan is very important to provide clear guidelines, and to make sure that all programs and initiatives will be conducted in a well-organized orchestration.