

Rebuilding Market Confidence
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ON CAPITAL MARKET REFORM IN ASIA
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Emerging markets must develop a comprehensive regulation and sophisticated market infrastructure so as to give protection to their investors and to create market confidence. It is a major issue in Indonesian capital market recently to rebuild market confidence to keep the momentum of the bullish market as reflected by the increasing of the market capitalization, investment fund and average composite Index.

The development of rule and regulation in Indonesia can not be separated from the story of the capital market itself. Therefore, before describing more detail about the regulation aspects, firstly, I will talk about the story of the Indonesian capital market.

The Indonesian Capital Market was reactivated in 1977 as Bapepam was established. It had been less active during the period of 1977 to 1988's, where the number of issuers listed in the Stock Exchange was just about 24 companies. However, there was a significant increase in the number of the issuers from 1988 to 1992 at 200's companies. Furthermore, at the end of 2003 the number of the issuers

has increased to around 360 companies, which are most of them issue shares and/or bonds.

Another interesting story is the development of the Indonesian capital market regulation, where it was more complete since 1990's. In the beginning of 1990's, the Indonesian Capital Market was regulated only by the Ministry of Finance decree. Nevertheless, since 1995 the Indonesian Capital Market has had stronger legal base as the Law No. 8 year 1995 concerning Capital Market was legislated by Parliament. Furthermore, it is being amended and waiting for the House of Representative's approval. Current Capital Market Law is implemented through two Government Regulations, seven Ministry of Finance Decrees, and more than 140 Bapepam's rules.

The following table is to give you an overview about the Indonesian Capital Market conditions as of 31 September 2003 :

(IDR 8,400 = USD 1)

		31 September 2003
Numbers of issuers	:	527 issuers
Market capitalization	:	IDR 396.02 trillion
Bond issuance value	:	IDR 35.96 trillion
Numbers of securities companies	:	191 companies
Numbers of investment fund	:	175 companies
Total Net Assets Value of investment fund	:	IDR 81.32 trillion
Numbers of stock exchange	:	2 (two), <i>Jakarta Stock Exchange</i> for securities instrument and <i>Surabaya Stock Exchange</i> for debt instrument.

In Indonesian capital market investment fund has increased dramatically from time to time. As we know that the investment fund is one of the means for retail and or small investor to participate in the capital market. It has already developed in Indonesia since 1996, where there were 25 investment fund with total asset value amounting to IDR 2.78 trillion at that time. Today, there are 175 investment funds amounting to IDR 81.32 trillion. It means that the investment fund has increased 7 times and 29,23 times interms of the Net Assets Value (NAV). The most single year that gave the significant constribution is in 2003. Where the Net Assets Value (NAV) in the beginning of 2003 was IDR 51,067.46 trillion, then it became IDR 85,851.87 trillion at the end of 2003.

There is a discourse in Indonesian capital market recently after Bapepam proposed a rule about the method to calculate the Net Assets Value (NAV) of investment fund portfolio based on marked to market valuation. The intention of it is to create the fair value of the investment fund portfolio so as to give the same methodology in calculating the investment fund portfolio among the investment manager.

The development of the Indonesian capital market is influenced by internal and external factors. Therefore, it is less complete if we don't take into account the external factors, such as the crisis that occurred in 1997 that hit most of the asian countries. The impact of the crisis is still exist until now in some countries in the region, especially for the

Indonesian economy that give indirectly bad influence to the capital market.

Another external factor was the World Trade Centre tragedy in September 11 2001 in New York, US. It did not only affect the US but also the world globally. In addition to the international security problems, the Indonesian capital market is also affected by domestic security condition, such as Bali bomb blasting and the recent blasting in J.W. Marriot Hotel, Jakarta.

As a regulator, I can not always hope that economic conditions and other factors, such as domestic security factor, are always conducive for capital market. What I have done is always try to create the transparent, orderly, and efficient capital market, in order it can attract local investor and foreign investor by providing regulations to support the goal. In other word, what I am trying to explain is how to rebuild market confidence that have been decreased as a result of external and internal factors of the capital market itself. In rebuilding the market confidence that have been up and down for the last 5 years, I have been doing 2 kinds of restructuring which are internal and external restructuring.

Firstly, I will discuss about the internal restructuring, which is the organization restructuring. Recently, the Indonesian government have been drafting a law concerning Financial Service Authority (FSA), the idea of the FSA is to merge 3 (three) authorities currently exist in Indonesia, which are the capital market authority (Bapepam), Indonesian

Central Bank and Directorate General of Financial Institution. Until now, the establishment of the FSA is still under discussion by the house of representative and the market player, regarding the advantageous and disadvantageous of the FSA.

It does not matter either Bapepam will join FSA or still under Ministry of Finance, as a chairman of Bapepam, my priority is to prepare a credible, independent and adaptable capital market authority enabling to catch a rapid capital market development. In achieving these goals, I have done 2 (two) kinds of restructuring, which are internal and external restructuring. As I mentioned above, the internal restructuring is concerning organization restructuring, which is the changing in the organization structure. It aims to strengthen the performing and function of Bapepam. I hope it will be implemented in April 2004. The major thought in designing the new structure of Bapepam is it will emphasis on some functions that are needed in order to strengthen the structure of Bapepam. At this moment, Bapepam has policy making, regulatory, licensing, supervisory, and inspection functions. In the new structure the policy making and supervisory function will be enlarged by adding some divisions, such as policy making division at Investment Management and Research Bureau and Market Institution and Transaction Bureau. Besides, there will be special division concerning policy, corporate governance and accounting compliance monitoring division.

In addition to restructuring its organization, Bapepam has always made effort to complete and make a comprehensive rule. One of the most important rules is a rule concerning Independency of Public Accountant. The rule was enacted as an anticipated action to prevent recurrence of accounting abuse of the financial scandal of big companies in the US, such as Enron, WorldCom and Xerox, that some people think that it was caused by the public accountant of the companies.

Based on the experience of the USA, disclosure principle in capital market must be sustained and improved. One of the implementation of the disclosure principle is through financial statement of a company audited by public accountant. In order to improve the quality of financial statement of issuers/public companies, it is highly needed an opinion or valuation of independent and professional parties. Therefore, the rule that was issued by Bapepam at the end of 2002 is concern on liabilities and prohibition that must be done, limitation of audit periods, and other non-audit services prohibited for public accountant in order to keep its independency. Besides, Ministry of Finance is also drafting law concerning Public Accountant. The goal of this law is to protect public interest, especially stakeholders of companies' financial statements.

On the other hand, Bapepam has also issued other regulation, such as regulation that requires the management of Issuer/ Public Company announce the auditor's reason when auditor's opinion of its

financial statement of a certain period is other than an unqualified opinion. This announcement,-- attached with the announcement of periodical financial statement,-- has a purpose for the company's stakeholders recognize the real condition of the company and to assist their investing decision in the future.

I will move to the second restructuring, which is external improvement. The first action that will be conducted is demutualization of Stock exchange. The primary reason of demutualization of stock exchange in Indonesia is the need to take a part in global competition, and also the need to behave in conformity with various innovation of information technology in capital market. We hope, with the sophisticated infrastructure, the stock exchange could develop its service and type of product that can attract investor, so that, it will be able to raise the liquidity. Besides, in globally competitive era, the management of stock exchange is required to create two capabilities, the sustainable of growth rate and competitiveness. To reach the goals, it is essential to improve some aspect related to the ownerships structure, the orientation, or the management of the stock exchange. In conclusion, with the demutualized structure and characteristic of the stock exchange will be conducive to create conditions needed to promote the growth rate and high competitiveness.

The process of demutualization of stock exchange in Indonesia has reached the final step and would be finalized simultaneously with the amendment of its based law, The Amendment of the Capital Market Law. Therefore, we will choose one of four forms of demutualization. They are Direct Demutualization, Investment Holding Company, Operating Holding Company Non Self Regulatory Organization (SRO) or Operating Holding Company SRO. The model of demutualization that would possibly be chosen is Operating Holding Company SRO. In this model, the stockholders of stock exchange will establish a holding company which is owned by the majority stockholders of the stock exchange.

Other aspect that we need to do is the improvement of the Securities Company. As I mentioned above, the number of securities company in the Indonesian capital market in September 30 of 2003 was 191 companies. It was relatively large number compared to other countries have such as Malaysia and Singapore. To strengthen the base of Securities Company, in May 8 of 2003, we promulgated the minimum level of securities company capital, as can be seen from the table below:

Figure

Type of activities	Phase I (31 Dec 2003)		Phase II (31 Dec 2004)	
	Working Capital	Net Adjusted Working Capital	Working Capital	Net Adjusted Working Capital
Underwriter	IDR. 25 Billion	IDR. 10 Billion	IDR. 50 Billion	IDR. 25 Billion
Broker-Dealer:				
• Non-administering Client Account	IDR. 500 Million	IDR. 200 Million	IDR. 500 Million	IDR. 200 Million
• Administering Client Account	IDR. 15 Billion	IDR. 20 Billion	IDR. 30 Billion	IDR. 25 Billion
Investment Manajer	IDR. 3 Billion	IDR. 200 Million	IDR. 5 Billion	IDR. 200 Million
Underwriter & Investment Manajer	IDR. 28 Billion	IDR. 10,2 Billion	IDR. 55 Billion	IDR. 25,2 Billion
Broker-Dealer-Administering Client Account and Investment Manajer	IDR. 18 Billion	IDR. 10,2 Billion	IDR. 35 Billion	IDR. 25,2 Billion

Through this forum, I intend to request all participants' opinion about the development of the Securities Company. In the analysis of development of the Securities Company, we use a series of study analyzing some relevant variables that includes clients, human resource, Financial Condition, BOFIS, Risk Management, Compliance, Net Adjusted Working Capital, and transaction. Then, the securities companies are divided into 6 categories considering securities company business specification and homogenous condition.

Grade 5 or 6-securities company consists of 40 securities companies that have 61.33% transaction in exchange in 2001. This characteristic of Securities Company in this group can represent a preliminary model of an ideal securities company and lay out basic requirement for exchange member.

Securities Company that is in grade of 4,3,2,1 and NA consist of 164 securities companies that have 31.62% transaction in the exchange in 2001. These companies can still handle client account and become Exchange member by improving their capital structure, Net Adjusted Working Capital, BOFIS, human resource, and or merging with other securities company. They can also choose to become a non-Exchange member that does not manage clients' account and forms up a mutual co-operation with exchange member.

Because this forum will also discuss the implementation of Good Corporate Governance Principles in the regional territory, at the end of this speech, I will explore its implementation in Indonesia. Until now, Indonesia has a national guideline of Good Corporate Governance. We wish that all companies that are established based on Indonesia law and regulation would implement this guidelines promulgated by NCCG. It can be started by public company--listed or non-listed public company, then state-owned company, and company that is financed and manages public fund, and so on.

Specifically, there is no Bapepam Rule that directs the implementation of Good Corporate Governance. However, most of all principles of Good Corporate Governance, such as transparency, fairness, responsibility, and accountability, have been implemented into Bapepam Operational Regulation. E.g.: Bapepam Rule concerning disclosure of information on financial reporting, material transaction, conflict of interest transaction, tender offer, merger, and take over, procedure of share holder meeting and independency of accountant.

To compare rules that relate to the implementation of Good Corporate Governance in the regional territory, let me compare the content of White Paper on Corporate Governance in Asia established by Roundtable Meeting with the Bapepam's Operational Rules. As we all have known, the drafting of this white paper was focused on some important issues. They are: Shareholders' Rights and the Equitable Treatment of Shareholders, the Role of Stakeholders in Corporate Governance, Disclosure and Transparency, and the Responsibilities of the Board. All of these primary issues have been implemented on Bapepam Operational Rules as I mentioned before.

As the Capital Market authority, all the effort that can be done by Bapepam are only create a facility in the form of regulation, hopefully it can support and improve an ordinary, fair and efficient capital market, and as the result it can recover the market confidence that it has already lost for long enough. I believe that with the clear regulations all the goal

can be achieved. It was supported by the fact that the Indonesian capital market was still sustained under economic and socio politics crisis that hit Indonesia recently, it can be seen from the capital market indicator such as Composite Index of the Stock Exchange that reached the level 600 in the early of October 2003, market capitalization has also increased, and net asset value of investment fund has skyrocketed.

That is all my presentation. I would like to thank for this chance as the chairman of the Indonesian Capital Market Authority to discuss an overview outlook of the capital market.

Herwidayatmo,

Tokyo, November 19, 2003