GOOD CORPORATE GOVERNANCE: STRATEGY TO IMPROVE INVESTMENT IN INDONESIA’S CAPITAL MARKET

Mochammad Rosul
The Monetary Crisis in Asia →
Crisis in Indonesian Banking
↓
Waken the awareness of the
government and business actors
that excessive dependence on
banking as financial source was
very risky
↓
Banking sector → Capital market
**TABLE 1**
Sources of Funds for Indonesia’s Business Finance, 1991-2001 (Cumulative)

<table>
<thead>
<tr>
<th>Year</th>
<th>Bank Loans Rp trillion</th>
<th>Bond and Share Issues Rp trillion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>113.6</td>
<td>11.2</td>
</tr>
<tr>
<td>1992</td>
<td>123.7</td>
<td>15.0</td>
</tr>
<tr>
<td>1993</td>
<td>148.3</td>
<td>21.8</td>
</tr>
<tr>
<td>1994</td>
<td>188.9</td>
<td>33.2</td>
</tr>
<tr>
<td>1995</td>
<td>234.6</td>
<td>44.1</td>
</tr>
<tr>
<td>1996</td>
<td>293.0</td>
<td>61.5</td>
</tr>
<tr>
<td>1997</td>
<td>378.1</td>
<td>89.6</td>
</tr>
<tr>
<td>1998</td>
<td>545.4</td>
<td>94.8</td>
</tr>
<tr>
<td>1999</td>
<td>277.3</td>
<td>229.9</td>
</tr>
<tr>
<td>2000</td>
<td>320.4</td>
<td>254.8</td>
</tr>
<tr>
<td>2001</td>
<td>358.6</td>
<td>263.0</td>
</tr>
</tbody>
</table>

*Source: Central Bank of Indonesia*
<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Shares</th>
<th>% Change</th>
<th>Transaction Value</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992</td>
<td>1,089,456,792</td>
<td>--</td>
<td>2,095.2</td>
<td>--</td>
</tr>
<tr>
<td>1993</td>
<td>3,844,031,699</td>
<td>252.84</td>
<td>19,086.2</td>
<td>810.94</td>
</tr>
<tr>
<td>1994</td>
<td>5,292,580,825</td>
<td>37.68</td>
<td>25,482.8</td>
<td>33.51</td>
</tr>
<tr>
<td>1995</td>
<td>10,646,444,247</td>
<td>101.16</td>
<td>32,357.5</td>
<td>26.98</td>
</tr>
<tr>
<td>1996</td>
<td>29,527,727,838</td>
<td>177.35</td>
<td>75,729.9</td>
<td>134.04</td>
</tr>
<tr>
<td>1997</td>
<td>76,599,170,013</td>
<td>159.41</td>
<td>120,385.2</td>
<td>58.97</td>
</tr>
<tr>
<td>1998</td>
<td>90,620,529,970</td>
<td>18.30</td>
<td>99,684.7</td>
<td>-17.20</td>
</tr>
<tr>
<td>1999</td>
<td>178,486,582,779</td>
<td>92.55</td>
<td>147,880.0</td>
<td>48.35</td>
</tr>
<tr>
<td>2000</td>
<td>134,531,333,895</td>
<td>-22.90</td>
<td>122,774.8</td>
<td>-16.98</td>
</tr>
<tr>
<td>2001</td>
<td>148,381,308,944</td>
<td>10.29</td>
<td>97,522.8</td>
<td>-20.57</td>
</tr>
</tbody>
</table>

Source: Indonesia Capital Market Supervisory Agency.
Constraints on the role and function of the capital market in Indonesia i.e.:

✓ The relatively small capitalisation of the Indonesian market compared to its competitors.

✓ Investor institutions, which are expected to play a strategic role in this effort, have turned out to be unfamiliar with or reluctant to invest in the capital market.

✓ The low level of compliance by companies with the principles of good corporate governance.
Strategy for capital market development i.e.: 

✓ Improving compliance with good corporate governance practices.

✓ Harmonization of rules and institutions.

✓ Integrated development of information technology and human resources.

✓ Implementation of safety and service quality conforming to international standards.

✓ Development of market and capital market instruments.
Inadequate framework for corporate governance in Indonesia, reflected by:

✓ Non-optimal regulator to control issue regulation

✓ Minimum standards concerning reporting company performance and company liabilities

✓ Inadequate supervision of management due to lack of independent directors and doubts about the independence of auditors

✓ Limited rule compliance mechanism as well as legal enforcement.
The above problems have resulted in inadequacy of information for risk analysis/results, excessive investment in unproductive resources, which unsettle market confidence

Efforts to solve the problem are needed

Reforming corporate governance practices and applications in the capital market
The condition of corporate governance in Indonesia:

- Indonesia ranks among the worst in standards of auditing and compliance, accountability to shareholders, standards of disclosure and transparency, and Board processes.

- The degree of investor protection in Indonesia is the lowest in Southeast Asia.

- The ownership of listed companies is highly concentrated, and the percentage of managers belonging to the controlling group is also very high.

- Control mechanisms (‘checks and balances’) have been lacking.
✓ Transparency has been poor as disclosure practices, accounting standards, and their implementation have been inadequate

✓ Legal protection has been weak due to the inefficient judiciary system
Efforts to improve corporate governance in Indonesia’s Capital Market:

A regulatory framework has been formulated (rules & regulations issued by BAPEPAM):

• Prohibition of Insider Trading
• Rule on Information that must be Disclosed Immediately
• Rule on Disclosure of Certain Shareholders
• Rule on Tender Offer
• Rule on Conflict of Interest
• Rule on Material Transactions and Change in the Line of Business
• Rule on Mergers and Consolidation for Public Companies

• Rule on Acquisition of Public Companies
✓ BAPEPAM Rule No. III A.3 regarding Commissioners and Directors of Stock Exchange has been revised

✓ Enforce by imposing administrative penalties and ordering certain measures, i.e,
  · Suspected market manipulation and insider trading of PT Indosat and sale of shares in BCA Bank and Semen Gresik.
  · Suspected violation in transactions of shares of HM Sampoerna in immediate market.
  · Suspected violation against transparency of information
  · Co-ordination with the SROs (Self Regulatory Organizations), Police Department, Public Prosecutor and Capital Market Supervisory Institutions of other countries
✓ BAPEPAM actively publicized the plan to revise capital market rules

✓ Up to June 2002, BAPEPAM had issued warning letters to some issuers

✓ An Indonesian Market Board of Arbitrage (BAPMI) has been established

✓ Restructuring of Indonesia’s Stock Exchange (the Bourse), the Clearing and Guarantee institution (CGC), and the Central Securities Depository (CSD)

✓ BAPEPAM developed an e-Reporting System in co-ordination with SROs.
AEI actively participated by

- Publicizing the objectives of implementing good corporate governance implementation

- Giving direct as well as indirect information to members about the capital market rules

- Studying related rules and providing input and suggestions for modification where necessary

- Periodically up-grading its members, to carry out lobbying

- Doing public relation works to communicate the results of good corporate governance implementation to involved parties as well as to the general public