

WELCOME ADDRESS

Twelfth Asia-Pacific High Level Meeting on Banking Supervision

Jointly organised by the Basel Committee on Banking Supervision (BCBS), the Financial Stability Institute (FSI), and the Executives' Meeting of East Asia-Pacific Central Banks Working Group on Banking Supervision (EMEAP WGBS), hosted by Bank Indonesia

"Taking stock of post-crisis regulatory reforms in Indonesia – progress made and challenges ahead"

Bali, Indonesia, 22-23 March 2017

Remarks by Mr. Erwin Rijanto, Deputy Governor of Bank Indonesia

Honorable

- **Mr. Fernando Restoy, Chairman FSI, BIS**
- **Mr. Nestor A. Espenilla, Chairman EMEAP WGBS and Deputy Governor Bank of Sentral Ng Pilipinas,**
- **Mr William Coen, Secretary General BCBS, BIS**
- **and fellow delegates from financial stability authorities and representatives of the financial industry**

Good morning to all of you,

1. It is my pleasure to welcome you to the 12th Asia-Pacific High Level Meeting on Banking Supervision. Together with the Bank for International Settlement and EMEAP, Bank Indonesia is honoured to host this event in the beautiful island of Gods.
2. In my welcome address today, I will slightly touch upon the global financial sector reform initiatives to give a flavour of the speech and emphasize more on the progress and challenges in Indonesia. I would like to highlight that the progress so far is due to the joint efforts of relevant authorities and the support from the industry.

Ladies and Gentlemen,

3. The costs of the financial crisis are significant. According to the Financial Stability Board (FSB), the cumulative loss of output since the crisis, compared to its pre-crisis trend, is estimated around 25% of one year's world GDP.
4. To address the fault lines that caused the financial crisis, the G20 Leaders in 2008 agreed to initiate a comprehensive programme of regulatory reforms which covers 4 (four) core elements: 1.) Building resilient financial institutions; 2.) Ending too-big-to-fail; 3.) Making derivatives markets safer; and 4.) Transforming shadow banking into resilient market-based finance.
5. As a member of the FSB and the Basel Committee on Banking Supervision (BCBS), Indonesia endeavours to implement the reforms in a full, timely and consistent manner albeit challenges due to differences in the characteristic of our financial market with that of advance economies, in which the regulation is build upon.

Ladies and Gentlemen,

6. **Building resilient financial institutions.** The first element of reforms centered on the Basel III package. The quality and level of capital has been increased and new standards for liquidity has been introduced. In addition, leverage has been constrained and explicit macroprudential dimension has been introduced.
7. Although we started a year late, Basel III implementation in Indonesia has been in accordance with BCBS phase-in arrangements since 2014. I am pleased to inform you that Indonesian banks are not facing significant challenges, especially with regards to the capital reform, due to the high levels of capital ratio dominated by Common Equity Tier 1. Indonesia has also

implemented the countercyclical capital buffer and capital conservation buffer in addition to the minimum capital requirement.

8. In terms of Liquidity Coverage Ratio, banks that are required to adopt the standard have no major difficulties complying. Nonetheless, we continued to monitor the long run impact of the requirement.
9. **Ending too-big-to-fail.** The next core element is ending too-big-to-fail. A set of measures, known as the Systemically Important Financial Institutions (SIFI) Framework, has been introduced.
10. Although Indonesia is not home jurisdiction of the Global Systemically Important Banks, a number of domestic banks are required to meet capital surcharge that varies between 1% to 2.5% to reflect their systemic importance in the domestic financial system.
11. Indonesia has also passed the Law on Prevention and Resolution of Financial System Crisis in April 2016. The law enables related financial stability authorities to implement a more rigorous banking regulation and supervision, particularly for Domestic Systemically Important Banks, including the provision of recovery plans. It also provides legal foundation of bail-in mechanism.

Ladies and Gentlemen,

12. **Making derivatives markets safer.** The third fundamental area of reform is in the OTC derivatives market. The crisis highlighted how the opaque inter-connections across financial institutions engaged in trading complex derivative contracts over-the-counter and poor risk management led to rapid contagion and systemic crisis.

13. The reform has focused on 5 (five) areas: standardization of derivative contracts; platform trading; central clearing; higher margin and capital requirements for non-centrally cleared trades; and mandatory reporting of all trades. Indonesia has implemented reporting requirement for banks engaging in OTC derivatives transactions. In addition, platform trading are required for both equities and commodities derivatives. National authorities are also in the proses of establishing a CCP for OTC derivatives. This step would complement the higher capital requirement for Non-Centrally Cleared OTC derivatives regulation issued in September 2016.
14. **Transforming shadow banking into resilient market-based finance.** Compared to other elements of the reform, internationally-wide implementation of the agreed reforms related to shadow banking remains at relative early stage. The FSB and jurisdictions are planning to conduct more work to assess and respond to potential financial stability risk in this area.
15. With regards to monitoring and regulation of non-bank financial entities (NBFEs), the Indonesian FSA is responsible to supervise these institutions. It also has the authority to pass regulations on new and existing NBFEs activities. Bank Indonesia also performs periodic assessments of emerging non-bank financial intermediary activities from a macroprudential perspective. Efforts to reduce gaps between the risk assessment framework for NBFEs and the banking system are on-going.

Ladies and Gentlemen,

16. Implementation of the reforms is challenging. Of importance, is ensuring that the implementation of the regulatory reforms does not impair the ongoing economic recovery process and that resilience of the banking system is preserved.

17. We noted several challenges need to be address. First, with regards to **BCBS review of the regulatory treatment of sovereign risk**. We underline the need to undertake due consideration on the important role of sovereign debt in monetary operation, the financial market and economic development financing, especially in emerging economies. A one-size-fits-all approach may not be suitable due to different sovereign instrument and financial market characteristics among regions.
18. Second, **revision on the standardized approach for credit risk and market risk**. BCBS is working on revising the standardized approaches for credit risk and has revised the framework for market risk to enhance robustness and risk sensitivity of both framework. Consequently, the standardized approach will be more granular and complex. On the other hand, Indonesian banks mostly engage in traditional banking activities. Hence, regulators and the industry will need to adjust their skills and information system accordingly.
19. Last but not least, **as a number of regulatory reforms are finalized**, member jurisdictions including Indonesia are expected to implement these reforms expeditiously according to the committed time line. Given limited resources, authorities will need to strengthen coordination to ensure full and timely implementation.

Ladies and Gentlemen,

20. I have no doubt the 12th Asia-Pacific High Level Meeting on Banking Supervision will be fruitful as we have an excellent line of speakers, who will be deliberating current and critical issues in Supervision and Banking in this post crisis era.
21. I believe there is no right or wrong when discussing frameworks for effective supervision and banking regulation. The effectiveness of the agreed standards depends on many aspects and that there is no

one-size-fits-all approach. As many have said: "Economics is the only field in which two people can get a Nobel Prize for saying the opposite thing" is true.

22. Before I close my welcome address, allow me to offer my warmest welcome to you all and express my deepest gratitude to your visit. I hope you will make the most of your stay in Bali and take home with you warm memories of your visit.
23. I would also like to remind you that Indonesia will be hosting IMF – World Bank Annual Meeting on October 2018 in this beautiful island of Bali. I would like to invite you to visit Bali, not only to attend the workshops, but also to participate in a series of activities in connection to the Annual meeting. Please save the date, and mark your agenda.

Thank You.