

Challenges in Effective Application of the Indonesian Capital Market

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Abstract—*Capital market is an indicator of a country's economic progress. The existence of the Indonesian capital market has experienced ups and downs that can be seen from the fluctuating IHSG indicator. It is a result of globalization and economic integration that leads to the performance of the capital market depends heavily on the performance of the national, regional and international economy. The role of local investors is greatly needed to encourage the Indonesian capital market to be more resistant to various crises and shocks. The population of Indonesia's middle class that has grown relatively large is an opportunity to encourage the investment in the capital market. Meanwhile, some challenges in the development of capital markets must also be overcome, such as the limited types of securities traded, rules for protecting investor rights, "games" in stock transactions and lack of public knowledge about the capital market. The objectives of this study are to maximize capital market opportunities as a driver of the Indonesian economics wheels and contribute to tax revenue for Indonesia and make the digital market the most efficient investment tool in terms of implementation and regulation in the future practice. This study uses the literature study method based on several previous studies and scientific journals that discuss the development of the Indonesian capital market. The results of this study are expected to be a consideration for the government and capital market financial supervisory institutions in making good and efficient system and transaction regulation for the Indonesian capital market.*

Keywords—*Indonesian Capital Market, Challenges, Regulation, Efficiency.*

I. INTRODUCTION

The Indonesian capital market is a growing market in which its development is very vulnerable to general macroeconomic conditions and global economic conditions as well as world capital markets. Economy does not affect the company's performance immediately but slowly and over a long period of time. Conversely,

stock prices will be affected immediately by changes in macroeconomic factors since investors react faster. When macroeconomic changes occur, the investors will take into account both the positive and negative impacts on the company's performance in the next few years before making a decision to buy, sell or hold the relevant shares. Therefore, stock prices are faster to adjust to changes in macroeconomic variables than the performance of the company concerned.

The composite stock price index as an indicator of the development of the Indonesian capital market, which is now called the Indonesia Stock Exchange (IDX), proves that the macroeconomic and global economic conditions cause the JCI to experience a movement that is closely related to the situation. Another factor that also influences the JCI movement is the country's political and security conditions. This paper discusses the history, development and challenges of the Indonesian capital market in the future.

Capital market is a non-bank financial institution also known as the Non-Bank Financial Industry (IKNB). The problem faced by Non-Bank Financial Industry (IKNB) is that the capital market is not well-known by the public for the low literacy about it. As an illustration, based on the results of a survey conducted by OJK to 100 respondents, only 7 people claimed to know the capital market or only 7% of the public understand capital market investment.

In addition to the lack of public understanding of the capital market, other problems may include lack of literacy, socialization, access to information, and access to capital market investments. Not to mention, the high number of foreign investors compared to local investors is a major problem in this study. Records of data from Indonesia's central securities custodian as of July 2016 based on the composition of total share ownership, foreign investors dominated the share ownership percentage of 64%, leaving local investors account only for 36%.

To improve the performance of the capital market in Indonesia on an ongoing basis, the policy makers should have taken advantage of the opportunities that exist in the Indonesian economy. One of the opportunities that

need to be utilized by stakeholders of capital market policy is the increasing middle class in Indonesia. The growth of the middle-class population in Indonesia is relatively high.

The objectives of this study are to maximize capital market opportunities as a driver of the Indonesian economics wheels and contribute to tax revenue for Indonesia, as well as provide input on how all stakeholders will be able to make the capital market as the most efficient means of investment and regulation in the future.

II. LITERATURE REVIEW

A. Capital Market

Capital market in a narrow sense is an organized physical place of traded securities called the stock exchange. Understanding the stock exchange is an organized system that brings together sellers and buyers of securities carried out directly or indirectly. According to the Capital Market Law No. 8/1995 on Capital Markets, [2] defines capital market “as the activity concerned with the public offering and trading of securities, public companies relating to the securities issued, as well as institutions and professions related to securities”.

Siamat defines capital market as an organized place and traded securities called stock exchanges. Stock exchanges are organized systems that bring together sellers and buyers of securities carried out both directly and through their representatives. The functions of the stock exchange include maintaining market continuity and creating reasonable securities prices through supply and demand mechanisms. The definition of capital markets in a broad sense is a concrete or abstract market that brings together parties who offer and need long-term funds, namely the period of one year and above. [3]

The definition of capital in general is a meeting place for sellers and buyers to make transactions in order to obtain capital. Sellers in the capital market are companies that need capital (issuers), so they try to sell securities in the capital market. Whereas buyers (investors) are parties who want to buy capital in a company that they think is profitable. [4]

B. Stock

In simple terms, stocks can be defined as a sign of the ownership or ownership of a person or entity in a company. Share is a piece of paper that explains that the owner of the paper is the owner of the company issuing the paper. Buying stocks is like saving money. The benefit that will be obtained by the ownership of shares is the ability to provide unlimited profits. It does not mean the profits of ordinary stock investment are very large but depending on the development of the publishing company. If a publishing company is able to generate big profits, it is possible that the shareholders

will enjoy big profits since big profits provide big funds to be distributed to shareholders as dividends.

Stock gives the possibility of unlimited income. Accordingly, the risk borne by shareholders is also high. Investment has the highest risk because investors have the last claim right, if the company issuing stocks goes bankrupt. Normally, it means that outside of bankruptcy, the potential risk faced by investors is only two, namely not receiving dividend payments and suffering from capital loss. Another advantage is that capital gains will be obtained if there is an excess selling price above the purchase price. There are rules that must be implemented to get capital gains; one of them is buying stocks when the prices go down and sell them when prices rise.

C. Bonds

Bonds are securities or certificates that contain contracts between lenders and loan recipients. Bonds are papers stating that the owner of the paper provides a loan to the company issuing the bonds. Basically, having bonds is exactly the same as having time deposits. Therefore, bonds can be traded. Bonds provide a fixed income in the form of interest paid in a fixed amount of predetermined time. Bonds also provide the possibility to get capital gains, namely the difference between the selling price and the purchase price. The difficulty in determining bond income is due to the difficulty of estimating the development of interest rates. Bond prices are very dependent on the development of interest rates. If bank interest rates show an upward trend, bondholders will suffer losses.

Besides facing the risk of developing interest rates that are difficult to monitor, bondholders also face capability risk, i.e. repayment before maturity. Before a bond is offered in the market, it is first rated by an authorized agency. The rating is referred to as a credit rating which is a risk scale of all traded bonds. This scale shows how secure a bond is for investors indicated by the ability to pay interest and repay the loan principal.

D. Preferred Shares

Preferred stock is a hybrid between bonds and common stock; besides having bond characteristics such as fixed result, it has also common stock characteristics. Usually, preferred shares provide certain options for dividend distribution rights. There are preferred shares buyers who want dividend receipts that have a fixed amount every year, some want to prioritize dividend distribution, and so forth.

The choice to invest in preferred shares is driven by the privilege of this investment tool, i.e. to provide more definite income. Even, the possibility of the profit is greater than the deposit interest rate if the issuing company is able to generate big profits, and preferred shareholders have the privilege of obtaining dividends that can be adjusted with interest rates.

III. RESEARCH METHOD

This study uses the literature study method, based on several previous studies and scientific journals that discuss the development of the Indonesian capital market. There are more than fifty international journals combined for the completion of this paper. The results of this study are expected to be a consideration for the government and capital market financial supervisory institutions in making good and efficient system and transaction regulation for the Indonesian capital market.

IV. DISCUSSION

A. 4.1 Development of Indonesian Capital Market

The Indonesian capital market has now developed into one of the long-term sources of funding for the business world and government. Various programs such as infrastructure development are also encouraged to use funding from the capital market.

The government is intensively carrying out infrastructure development such as ports, toll roads, power plants, railroads, airports, and everything that certainly need no small amount of funds in which relying on the State Budget (APBN) alone is not enough. The APBN available in five years is estimated at only Rp1,500 trillion. Meanwhile, the development needs are predicted to be more than IDR 5,000 trillion.

One of strategies that is currently selected is the use of various financing instruments in the capital market sector such as stocks and bonds. Various investment instruments include the Infrastructure Investment Fund in the form of KIK, Asset Backed Securities (EBA), Limited Investment Funds, Target Time Mutual Funds, etc.

In the future, the Indonesian capital market will also be more mature to compete, both in terms of capital market literacy, products, and in establishing cooperation between stakeholders. The Indonesian capital market will also be increasingly ready to compete globally.

B. 4.2 Constraints of the Capital Market Industry in Indonesia

The Indonesia Stock Exchange (IDX) reveals that there are several obstacles that will be experienced in the development of the capital market industry. First, financial literacy and even understanding of financial literacy are still small. As a consequence of globalization and economic integration, the performance of the capital market is highly depended on national, regional and international economic performances. The growth rate of the capital market is also determined by various macroeconomic indicators such as inflation rates, interest rates, exchange rates, and the magnitude of other macro indicators.

This is an important foundation for future capital market growth because it will determine the extent of

the rate of growth of the capital market. Some economic indicators that affect the performance of the capital market include interest rates, inflation rates, and exchange rates. Regional economic development in the Americas, Europe and Asia will also affect the world economy. Likewise, the debt crisis that hit countries in the European Union such as Greece, Portugal, Italy and others can adversely affect other economic regions.

One of the challenges of capital market performance is the growth of transactions on the secondary market. The stock market in Indonesia has experienced very good performance growth as can be seen from the growth of the stock price index. When the subprime case in 2008, the stock price index experienced a very sharp decline, almost touching the 1,100 level. For this reason, a sweetener is needed so that the secondary market continues to be passionate in transacting. As one of the countries with the largest population in the world, the increase in local investors is one of the factors that contribute to strengthen the market's resilience due to the short-term volatility of the flow of funds. With a large and strong local investor base, the Indonesian capital market is better prepared to face the 'shock' of the market. For this reason, education and socialization are the media that must be continuously developed.

Improved implementation of good governance and business ethics must also continue. History proves that neglecting the implementation of good governance has an impact on the decline in performance, reputation, and crisis. The cost must be paid each time dealing with the crisis, both the banking crisis of 97/98, the subprime crisis of 2008, and other crises with different dimensions and on a smaller scale. However, all parties must realize that good governance is the key to the sustainability of financial and capital market businesses. In addition, in other contexts, it also faces reputational risks associated with several issues in banking such as customer funds, etc. The point is how to implement good governance through the implementation of risk management and enforcement of rules so that financial businesses prioritize business ethics.

C. 4.3 Efforts to Achieve an Efficient Indonesian Capital Market

Capital markets are efficiently interpreted in different ways with different objectives. The capital market is defined as a market that normally provides services needed by investors with minimal costs. Capital market efficiency is a market where the prices of all traded securities reflect all available information (Tandelilin, 2007). [5]

Some conditions that must be met to achieve an efficient market are:

1. There are many rational investors that try to maximize profits,
2. All market participants can obtain information at the same time in an easy and inexpensive way,

3. Information that occurs is random,
4. Investors react quickly to new information, so the price of securities changes according to changes in the actual value of the information.

The basic concept of an efficient capital market is a byproduct of the research by Maurice Kennedy with the subject of research into the behavior of commodity and stock prices. The goal is to separate the regular price cycle, but he cannot find the cycle. Prices seem to follow a random walk which means that price changes in the past cannot predict price changes in the future. Increase and decrease in stock prices are in accordance with information received in the capital market.

The requirements for a stock market to be efficient include:

1. Information disclosure. Information is not held up or monitored (disseminated by certain parties) and can be obtained by the public without any cost involved in obtaining information for market participants.
2. Decreasing prices are freely. Prices are not monitored by any party whether the buyer or seller of shares. They cannot influence prices, and they are also prohibited from manipulating prices by law.
3. The market is always in balance. If the market is always efficient, the market will always be different in balance.

V. CONCLUSION

Capital Market has an important role for the economy of a country. The development of the Indonesian capital market in terms of several indicators

shows a rapid development in recent years. For the company, the capital market also provides a big advantage, i.e. to develop its business by using funds from the sale of shares in this market without having to pay a debt to the bank having quite high interest and complicated conditions. This market is also a leading indicator of a country's economy. If conditions are good or developing, the economy of a country will also be good.

Awareness of the importance of the role of the capital market for national economies should be our common task to immediately provide socialization, as well as education to broaden the public's knowledge about the capital market. For capital market supporting institutions, it is necessary to increase its contribution to the progress of the capital market in accordance with their respective functions.

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