Financial Technology:

*Managing Risks and Regulations to improve Indonesia’s Fintech Services Sector*

Financial literacy in Indonesia remains relatively low despite the rising middle class, which now makes the largest group of social pyramid in the country, accounted for 74 million people in 2014 and projected to be at 141 million people by 2020 (Boston Consulting Group 2014). Indonesia's financial literacy such as bank savings, the ability to find the right investment opportunities, the anticipation of future financial needs, and the general knowledge about health and life insurance is among the lowest in South East Asia.

Currently, only about 36 percent of Indonesian adults have a bank account, according to the Indonesian FinTech Association report (2016). The World Bank Findex also finds that only 27 percent of the Indonesian population save money at financial institution in 2014, only 7 percent receive wages via a bank account, about 9 percent use a debit card to make payments, and almost half of the population still borrow money through non-banks mechanisms such as from family, friends, and other forms of informal lenders. For a more advanced financial services such as insurance, the Indonesian Life Insurance Association reports that life insurance penetration is about as low as 2 percent of the population. Many people still perceive that getting insured is a complex process in terms of buying the insurance products to claiming them.

On the other hand, the internet penetration in Indonesia has experienced a sharp increase over the years. The most recent survey from the Indonesian Internet Service Providers Association (APJII) find that internet penetration has reached 51 percent of the population in 2016 (132.7 million people), about a 44 million increase from 2014. Furthermore APJII 2016 finds that about 70 percent of all internet users access the web via their mobile phones, and e-Marketer data shows that Indonesia is in the 7th position among countries the most smart-phone users. Seeing the rapid growth of internet and smart-phone users, it could be concluded that internet-based technology has the potential to increase financial inclusion in Indonesia.
In terms of insurance services, for example, technology could provide a different experience for both the provider and consumer. Technology could shorten insurance buying processes from 16 steps to just under 6 steps, which significantly cuts down processing time. With the technology being more familiar to the younger generation, this means that the market of insurance services in Indonesia could be potentially huge in the near future.

Other than low financial literacy, the financial technology (fintech) sector also faces other challenges, for instance, regulation adaptation is still relatively slow and many regulations are quite unclear. A great collaboration between the government and financial institutions are essential to find the best practices in the fintech industry. Furthermore, Indonesia has a lack of talents (engineer/developer) who understands the linkage between financial services and technology.

Overall, the low rate of financial inclusion and fintech shows that Indonesia actually has a large room for the financial technology sector to grow. The vast number of population and the rising middle class indicates that Indonesia is a promising huge market for the fintech and financial industry in general. Increasing awareness of banking services and fintech and as well as regulation reforms will help accelerate the growth and efficiency the fintech industry in the country.

**ISD Views**

The most urgent and important thing to do in the fintech sector right now is a clear regulation from the Government. Currently, the problem in the fintech sector is that it is handled by various government authority bodies ranging from the Bank of Indonesia (BI) to the Financial Services Authority (OJK); and there is also an involvement from the the Ministry of Communication and Informatics RI and the Ministry of Finance RI. It is important to note that the fintech sector should be led by one body in order to avoid inconsistent and conflicting regulations. At the end of the day, a clear, consistent, and conducive policy and regulation are what the fintech sector needs in order to grow and innovate.

Moreover, the policy and regulation should be inclusive, meaning that there is a synergy between mobile operators, banking sectors and delivery sectors. This should cover consumer protection mechanisms and an improvement in the National Logistics System (Sislognas) as well as an even distribution of ICT infrastructure development. And lastly, since talent in the fintech sector is scarce, investment in human resources development needs to be strengthened and leaning more towards supporting young generation and fintech business through, for example, awareness and access to grants and tax incentives.

Overall, the fintech industry is a relatively new economic sector that offers a great potential for economic growth despite currently confronted with numerous hurdles. An improvement in fintech sector means an improvement in a variety of other sectors such as financial, technology, e-Commerce, telecommunication, logistics and so on and so forth. For the next edition of ISSUES, we will address the result of ISD Council’s 9th Dialogue Series on “Managing Risks and Regulations to Improve Indonesia’s Fintech Sector”, which was held on February 16, 2017.
The President Jokowi-VP Kalla Administration has continued its efforts to improve national vocational schools (UMK) in the country. Recently, the Government has announced to carry out training programs to 15,000 teachers of SMK, which will be held in 17 work training centers (Balai Latihan Kerja/BLK) that are operated under the central government across the country. The lack of teacher quality remains one of the biggest challenges facing vocational schools in Indonesia. This is one of the contributing factors that lead to the current condition where many SMK (Vocational School) graduates are still lacking in skills when they enter the workforce.

Other than a hurdle in teacher qualification, another main issue is surrounding the effectiveness of the current curriculum. SMK’s curriculum is not following up with the needs of the industry in each local area. Ideally, vocational schools’ curriculum should inline, in which it goes along with the needs of the workforce in the local industry. Adjusting the curriculum with the needs of the local workforce means that strengthening the collaboration between SMK schools and the private sector is essential. To an extent, some vocational schools have been doing this. For example, SMK schools in the North Sulawesi province has adopted a thematic curriculum system, in which one of the focus programs is in the tourism sector, such as offering a Chinese language subject to respond to the increasing number of Chinese tourists visiting the region.

Curriculum reforms in SMK have been in the President Jokowi-VP Kalla’s agenda. The Government has planned to exempt vocational schools from the the National Examination (Ujian Nasional) as a way to strengthen SMK’s focus towards job training education system rather than theoretical. President Jokowi himself has recently criticized SMK’s curriculum for not having adequate training practices in its curriculum. He further points out that vocational schools should focus on teaching skills and keeping up-to-date with current technological change.

According to the Central Bureau of Statistics (BPS), the unemployment rate of those with vocational school diploma continues to climb up, reaching 11.1 percent in 2016, which accounts for 1.3 million people. In 2015, the number was at 1.1 million people. Contrastingly, the unemployment rate for general high school graduates (SMA) is at a lower rate of 8.73 percent in 2016. Ideally, the workforce with SMK diploma should have a lower unemployment rate compared to its SMA’s counterparts, as it is often the case in other countries such as Germany and South Korea.
ISD Views

Vocational schools are to a great extent needed (quantity-wise and quality-wise) in the midst of rapid infrastructure program under the current administration. Preparing the workforce to be ready to maintain soon-to-be completed infrastructures, for example, after the MRT project is completed, is not an easy task but it is essential for the sustainability in the long-term. Moreover, vocational schools in Indonesia are still very concentrated in Java Island and mostly limited to SMK. The number of Polytechnics are still well below other countries. To fill the vocational education gap in the quality of vocational schools, the collaboration between the Government and private companies needs to be strengthened. In addition to domestic companies, pursuing collaboration with foreign companies operating in Indonesia will further help improve the quality of vocational schools.

In addition to insufficient qualified teachers and facilitators, infrastructure in the vocational schools’ sphere is relatively still very lacking both in quantity and quality. Basic infrastructures such as school buildings and classrooms are often inadequate, and many old and shabby buildings are yet to be renovated. Identically, SMK’s infrastructure in terms of required facilities and tools for trainings and practices remain short and deficient. Many facilities are relatively not up-to-date with technological changes and well below international standards. This short supply of infrastructure both in quantity and quality is holding back SMK’s students from having their chances to properly study in vocational schools, and consequently making them unprepared to enter the workforce after they graduate. Fixing infrastructure problems is fundamentally needed in order to improve vocational schools in Indonesia.

Overall, job training programs such as vocational schools could help built a more skilled workforce in the Indonesian economy. Indonesia’s vocational schools will need to catch up with technological change and improve its educational training quality substantially. And lastly, considering the fact that SMK’s graduates have a higher unemployment rate than their SMA’s graduates counterparts, it indicates that vocational schools are in need of significant reforms and improvement, especially when it comes to linking between the specific skills and specific demands from the industry.

Feedback and input: rudhian@isd-indonesia.org or william@isd-indonesia.org