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Assessing Indonesia's Capital Market Reform Plan

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Indonesian capital market stands on the brink of a new era. Early this year, the Indonesia Composite Index (IHSG) climbed to a record high amidst a weakening Rupiah, defying deteriorating macroeconomic fundamentals. This anomaly prompted Morgan Stanley Capital International (MSCI), who already sent warning letters to Indonesian capital market authorities last year, to froze Indonesia's weighting in its index. It immediately led to a sharp fall in IHSG. The recent event revealed more than a typical shift in investors' sentiment, as it exposed deeper structural vulnerabilities within Indonesia's capital market.¹

The warning letter from MSCI served as a wake-up call for authorities to act decisively in strengthening the domestic market. In response, Indonesia's capital market authorities announced eight initiatives aimed at accelerating capital market reform. These initiatives

¹ Friawan, Deni. (2026). The Structural Fragility of Indonesia's Equity Market). *CSIS Commentaries*. CSIS Indonesia: Jakarta

consolidated into four key pillars: liquidity, governance, transparency, and synergy. They are collectively designed to address the long-standing challenge of limited market depth in Indonesia's capital market. Yet the real test lies in the details. Authorities and related stakeholders need to ensure that these reforms are well executed, aligned with public interest, and sustainable over time. Only then can the reform agenda restore investors' confidence and transform the capital market into an engine of growth.

Overview of Indonesia capital market positioning

Indonesia's market capitalization has grown significantly from ~ IDR 153 trillion in 1995 to ~ IDR 15,000 trillion in 2025.² However, comparing with its peers, Indonesia's capital market consistently recorded the lowest market size relative to its economic size (see Figure 1. Market Capitalization (as % of GDP) of ASEAN-5 Stock Exchanges, 1990-2023). According to CEIC Database, the market is still characterized by resource-heavy firms (~30% of total market capitalization), and financial services (~22%), which have volatile earnings, and GDP-like growth, respectively. This contrasts with Singapore, whose market is dominated by high-multiplier sectors such as technology companies. Furthermore, the small free float requirement and the dominance of state-owned companies (SOEs) limit valuation upside and market depth.

From Figure 2, the number of listed companies in Indonesia surged from ~100 firms in 1990 to ~900 in 2023, representing one of the strongest performances in expanding market access in the region. However, similar to other ASEAN countries, much of the stock market is still dominated by large conglomerates (Table 1). In terms of concentration rate, Indonesia top 10 companies (by market capitalization) accounted for 44% of total market capitalization and 33% of total trading value in 2023, remains high despite an improvement from 2015 position. This suggests that the capital market has not yet provided equal financing opportunities, resulting in firms' continued preference for banking lending as the primary source of financing.

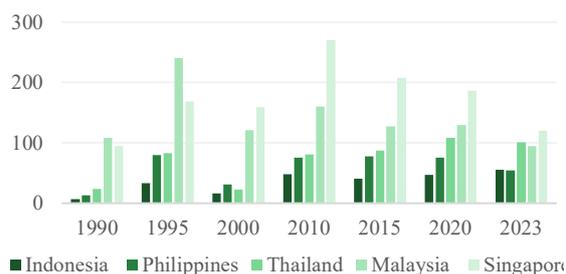
Based on Figure 3, Indonesia's capital market turnover rate has followed a persistent declining trend from 2000 and remain one of the lowest relatives to its peers. One of the main reasons is its small demand base. The number of equity holders represents only around 6-7% of total population, with merely about 0.06% of the population actively participates in the trading activities.³ Furthermore, given that Indonesians still dominated by informal worker (~59% of labor force) with limited financial literacy (~66% financial literacy rate), retail investors prefer to allocate their savings in cash, gold, and property.⁴ These assets perceived as relatively stable asset for their low risk tolerance and high-income volatility. In addition, pension funds and insurance companies face regulatory constraints on equity investment which limits long-horizon investment in the equity market. The combination of low retail participation and institutions' investment constraint have resulted in low liquidity in the domestic equity market.

² CEIC Database (2025)

³ Source: Indonesia Stock Exchange (IDX) (2025), Indonesia Financial Services Authority (OJK) (2025)

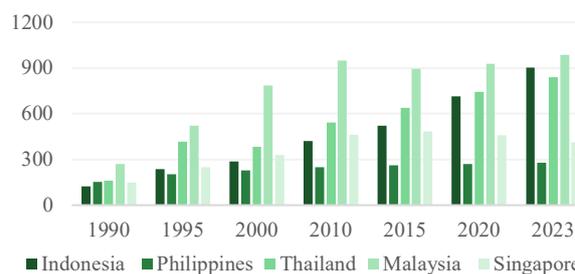
⁴ Source: BPS (2025) for informal workers, OJK's SNLIK (2025) for financial literacy rate

Figure 1. Market Capitalization (as % of GDP) of ASEAN-5 Stock Exchanges, 1990-2023



Source: World Bank (2023)

Figure 2. Number of Listed Companies on ASEAN-5 Stock Exchanges, 1990-2023



Source: World Bank (2023)

Table 1. Concentration Ratios of Listed Companies on ASEAN-5 Stock Exchanges, 1995-2020

	1995		2015		2020	
	(a)	(b)	(a)	(b)	(a)	(b)
Indonesia	58	53	49	74	44	33
Philippines	57	53	45	55	48	52
Thailand	48	31	33	69	34	68
Malaysia	35	18	34	64	31	68
Singapore	59	35	27	73	51	58*

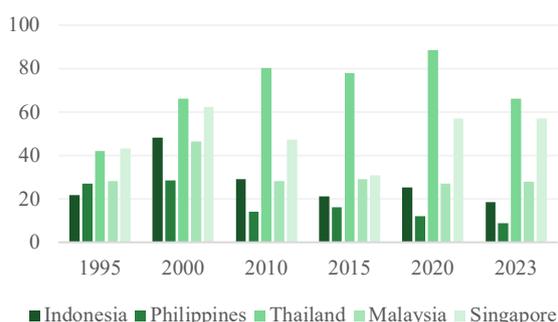
(a) : Top 10 Concentration Ratio (% of total market capitalization)

(b) : Top 10 Concentration Ratio (% of total trading activities)

* Singapore (2020) proxied by 2017 data

Source: FRED (2022), Indonesia Stock Exchange (2020)

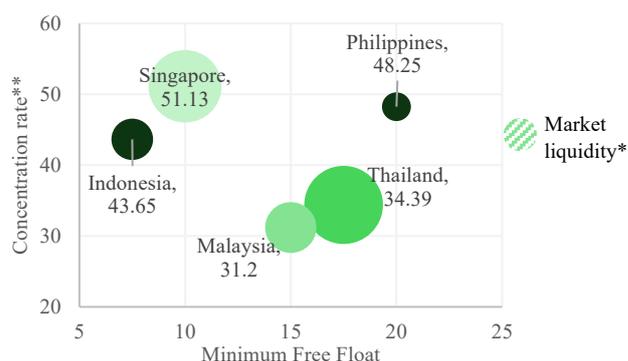
Figure 3. Turnover Ratios of ASEAN-5 Stock Exchanges, 1995-2023



Source: World Bank (2023)

* Singapore (2023) proxied by 2017 data

Figure 4. Free Float Threshold of ASEAN-5 Stock Exchanges, 2025



Source: IDX, PSE, Bursa Malaysia, SET, SGX⁵

* Market liquidity measured by market turnover

** Concentration rate measured by top 10 concentration ratio (% of total market capitalization)

⁵ PSE: Philippines Stock Exchange, SET: Stock Exchange of Thailand, SGX: Singapore Exchange

Liquidity: Raising minimum free float requirement from 7.5% to 15%

Indonesia's free float requirement is relatively low compared to other countries, regardless of similarities in ownership concentration and liquidity capacity (Figure 4). The low requirement has turned the market into a platform for rent extraction by large conglomerates and related parties, whose informational advantages and market power weaken incentives for retail and foreign investors to participate. In the absence of retail and foreign investors, market liquidity and turnover remains subdued, as trading is dominated by institutional investors who operate within predefined mandates rather than transacting freely based on market expectations. Thus, raising the free float requirement becomes a necessary step to encourage retail and foreign participation.

Following the increase in free float, a key question is whether Indonesia's capital market can absorb the estimated IDR 203 trillion of additional supply. Authorities seek to address this by raising the equity holding limit for pension funds and insurance companies from 8% to 20%, potentially adding around IDR 300 trillion if fully utilized.^{6,7} While this may help absorb the extra supply and reduce dependence on foreign flows, relying solely on these institutions risks beneficiary interests and remains insufficient to lift trading activity.

The jump from 8% to 20% would significantly alter the risk profile of funds managed by these institutions as it would raise exposure to capital market volatility. This could weaken institutions' ability to meet long-term obligations and adversely affect beneficiaries' investment outcomes. Therefore, the success of this policy hinges on the capability and credibility of fund managers to operate strictly within risk-based mandates. In addition, a gradual adjustment of the investment limit would help mitigate transition risks and allow institutions to strengthen their risk management system. Furthermore, policymakers should draw lessons from the 2019 insurance scandal, which affected 7 million policyholders, to recognize the importance of ensuring institutional readiness before implementation.⁸

On the other hand, the risk-based mandates governing pension funds and insurance companies constrain exposure to non-blue-chip stocks and limit flexibility in taking short-term positions. Thus, this initiative may have a limited impact on improving market turnover without complementary participation from retail investors, who could trade freely based on market expectations. As discussed in the previous section, authorities should not only improve the investment climate and strengthen investor protection but also work closely with the government to improve the job market and thereby raise disposable income. Once people have stable income, they are more likely to increase their risk tolerance and participate more actively in the equity market.

⁶ Indonesia Financial Services Authority (OJK)'s estimate (Kompas, Feb 2026)

⁷ Writer's estimate based on total stock holdings of insurance and pension fund which stood at IDR 229 Tn (IDX statistics, Aug 2025)

⁸ Indonesia audit board (BPK)'s estimate (Bloomberg, Jan 2020)

Governance: Demutualization of Indonesia Stock Exchange (IDX)

The Indonesian government has signaled plans to demutualize IDX since 2015, but the condition was not conducive at the time. The capital market size was relatively small, the legal framework under UU No. 8/1995 did not provide a clear legal basis for demutualization, and the supervisory capacity was still developing following the establishment of OJK in 2012. Now, with a larger capital market, more growth-oriented policy stance, and the enactment of the Financial Sector Development Law (UU P2SK), the timing appears more favorable for capital market transformation. However, with mixed outcomes coming from international demutualized exchanges, Indonesian authorities should proceed the demutualization plan with caution.

A notable example is PSE (Philippines), which struggled in the early years following demutualization. While most exchanges marked financial improvement, PSE's post-demutualization performance was weak. For comparison, the net income of ASX (Australia) increased from AUD 16.7 million in 1998 to AUD 59.1 million in 2002, whereas PSE's net income declined from PHP 70 million in 2000 to PHP 22.2 million in 2004 (Ho and Odhiambo, 2016). It was mainly due to the persistence of broker-dominated ownership in Philippines' market, which limit the governance reforms and market development. This illustrates that demutualization without meaningful ownership dilution and governance change is unlikely to achieve its intended outcomes.

On the other side, ASX (Australia) successfully delivered the commercial purpose of demutualization but struggling to deliver the social benefits. Demutualization transformed ASX into vertically integrated monopoly, as it controls trading, clearing, and settlement functions. Furthermore, the pricing authority and monopoly treatment were exercised under ex-post regulatory regime, resulting in the ability of ASX to increase fees charged to brokers and thus raise costs that were borne by end investors. This case suggests that demutualization success depends not only on ownership transformation but also on effective constraints of monopoly power.

Daya Anagata Nusantara Investments Agency (Danantara) plans to acquire IDX shares during its demutualization process. However, the execution of this plan could raise three potential conflicts of interest. First, this plan would transform Danantara into the owner of both the SOEs and the exchange, where SOEs' shares are traded. It could raise concerns among listed firms as to whether Danantara's oversight might unfairly favor SOEs. Second, as a Sovereign Wealth Fund (SWF), Danantara is a profit-oriented entity expected to generate positive and growing income each year. This stands in contrast with the exchange, whose primary role is to serve the public interests. Third, Danantara is a government initiative and thus, the possibility of preferential treatment towards firms closely aligned with the current government cannot be ruled out. If this happens, it will potentially incentivize domestic firms to list overseas, risking capital market deepening agenda.

To resolve potential conflicts of interest, the authorities should consider separating the regulatory and operational activities within the exchange. Initial experiences from international demutualized exchanges suggest several approaches, including transferring the regulatory functions to existing public authority or establishing a new regulatory body

specifically for the demutualized exchange. Regardless of the chosen option, the authorities must also ensure sufficient capacity and capability to carefully regulate, closely monitor the exchange, and decisively enforce the law are in place before demutualization. In addition, the authorities should clearly define a separate body responsible for appointing exchange directors and set limits on ownership concentration. All in all, these foundational arrangements should be clearly defined with the public interest as the primary consideration.

Transparency: Expand disclosure of share ownership to 1% and improve granularity of market data

The consortium of the Indonesian capital market (i.e., OJK, IDX, KSEI) plans to strengthen investor disclosure requirements to enhance transparency.⁹ First, the granularity of investor data will be expanded from 9 to 27 investor types. Second, the threshold for beneficial ownership disclosure will be lowered from 5% to 1%. The disclosure may signal government's commitment to regaining investors' trust, but it could also be excessive and impose significant administrative costs on all stakeholders. Compared with other countries, most report only around five investor types and maintain a 5% threshold for beneficial ownership. Furthermore, expanding disclosure requirements alone may not be sufficient, as authorities also need a well-defined plan and advanced systems to harness the data effectively.

Compared with other Asian countries, investor data in Indonesia is not effectively utilized.¹⁰ Market surveillance relies largely on manual monitoring and limited analytics, which hinders real-time detection of unusual trades. As a result, investigation and enforcement often take several weeks to months due to manual review and evidence-gathering challenges. Therefore, investment in advanced surveillance systems is necessary, but authorities must ensure that the associated costs are not passed on to end investors.

Authorities should also assess current laws and their enforcement to determine whether they provide sufficient deterrence against insider trading, so that the costs of providing high-granularity market data are not rendered ineffective. Current capital market law, UU No.8 of 1995, still defines the duty of trust over material non-public information as applying only to corporate insiders (e.g., directors, employees, lawyers, consultants), thereby creating loopholes for other parties who may also benefit from entrusted information, such as family members and friends (Niandita, 2024). This has resulted in limited law enforcement against insider trading conducted by relatives. One clear example is the difference in treatment between Monetary Authority Singapore (MAS), which applies insider trading provisions to all people who possess undisclosed information, and OJK in handling the insider trading of Bank Danamon (BDMN) acquisition plan in 2015.¹¹

OJK also faces challenges in tracing contraventions, establishing evidentiary proof from circumstantial evidence, as well as a trade-off between law enforcement and public interest,

⁹ KSEI: Indonesia's Central Securities Depository

¹⁰ As an example, SGX utilizes an advanced, real-time surveillance system called SMARTS to monitor any market misconducts, such as insider trading and manipulation. On average, it generates over 2,400 alerts monthly. (SGX Group, 2014)

¹¹ Kontan. (2015). Kasus insider trading saham BDMN dilepas <https://investasi.kontan.co.id/news/kasus-insider-trading-saham-bdmn-dilepas?page=all>

as aggressive enforcement may result in significant movements in the IHSG. Furthermore, the internal enforcement culture remains weak, with the level of law enforcement often depending on personnel assertiveness and initiative rather than the standardized processes.

According to Indonesia's criminal procedural law, the national policy criminal investigation agency (Bareskrim) also has the authority to conduct investigations related to capital-market cases. Examples include the investigation of PT Jouska Financial investment fraud and the recent IPO (Initial Public Offering) case of PT Multi Makmur Lemindo Tbk (PIPA). However, law enforcement efforts under Bareskrim also face some challenges, such as delays in information sharing from OJK and IDX, complex trading patterns and technical market dynamics that require advanced financial expertise, and a lack of jurisdictional clarity.

Therefore, in order to implement this initiative, authorities need not only compliance from investors, but also to improve their own surveillance system, redefine its legal framework, and build solid law enforcement. From there, the execution of this initiative is deemed efficient and beneficial for the public.

Synergy: Building stronger and mutually respectful coordination

The IHSG ultimately reflects the effectiveness of the capital market as an engine of economic growth. Accordingly, the success of capital market reform depends not merely on regulatory adjustments, but on policymakers' ability to address the structural constraints underlying market development. Market capitalization cannot expand sustainably if the economy has not transitioned toward higher value-added sectors with stronger growth potential and multiplier effects. Market liquidity will likely remain constrained as long as a large share of Indonesian workers face income volatility and possess limited financial literacy. Likewise, high market concentration may persist without meaningful improvements in legal certainty, governance standards, and law enforcement.

With the view in this light, the current reform agenda should not be treated as a narrow financial sector initiative, but as a broader opportunity to address foundational weaknesses in the economy. Its success hinges not only on stronger coordination within the consortium of capital market institutions, but also on effective policy alignment across government bodies and constructive engagement with the private sector.

At the same time, such synergy must respect institutional mandates and credibility. While some institutions are tasked with accelerating growth and deepening markets, others must safeguard macroeconomic stability and financial soundness during the reform process. Therefore, sustainable capital market reform requires balanced coordination in which growth objectives and stability considerations reinforce rather than undermine one another.

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