J.P.Morgan

Innovations to drive leadership in banking

As Indonesian companies expand into new markets, and as regulatory requirements continue to grow, financial institutions in Indonesia need to leverage new solutions and global expertise to manage their business better, amid increasingly dynamic and volatile economic conditions

While Indonesia has been an economic success story for more than a decade, the combination of lower commodity prices impacting one of the largest drivers of export growth, and slower policy implementation in the run-up to the 2014 elections, has resulted in growth unravelling. To avoid a repeat of the situation during the Asian financial crisis in 1997/98, the central bank has been proactive and has stepped up its use of policy tools through actions such as raising interest rates.

Even as the banking industry has remained one of the strongest engines of economic growth in this changing environment, the importance of the industry also means that it is under a magnifying glass more than ever. Banks are thus working to enhance their preparedness by raising their own interest rates in the wake of the central bank's proactive stance, and ensuring that they have a sufficient liquidity buffer to reduce the impact of non-performing loan issues they might face in a more challenging economy.

As local financial institutions (FIs) face the impact of compliance with anti-money laundering (AML), the Foreign Account Tax Compliance Act (FATCA) and the Office of Foreign Assets Control (OFAC) requirements, as well as the challenge of performing well in this more difficult economic environment, taking advantage of new leading-edge tools and global knowledge can also improve the performance of FIs and help ensure compliance.

Liquidity management account

With Basel III putting a price tag on the value of liquidity for the first time and with FIs wanting to grow operational account balances to ensure that they have a sufficient liquidity coverage ratio, banks are looking for leading-edge liquidity solutions. In response to the changing regulatory environment, one recent development is J.P. Morgan's liquidity management account (LMA), which allows clients to receive an enhanced rate of return on their operating cash balances. LMA pays term-like rates (up to six months) for balances that are stable in the account, thereby allowing clients to enjoy same-day liquidity and also receive enhanced rates for balances that are stable.

In the past, clients often used sweeps or invested overnight in commercial paper to increase their yield. LMA rewards clients for parking stable operating cash balances on a duration basis. By using LMAs, clients can enhance their yield based on stability of balances.

In the current economic environment, it is important for FIs to select their counterparty carefully and consider key differentiators such as the financial strength and credit rating of the global bank, and the reporting or other information the global bank can provide. With LMA, clients can view reports that clearly show various balance tiers established, fluctuations in balances and the resulting impact on tiers and yield. These types of reports provide valuable insights into changes in the account and enable better funds management.

While LMA is a relatively new concept, the take-up rate has been good and there is strong interest in the product given it enhances yields and assists with better forecasting, while maintaining adequate liquidity at all times.

Managing foreign exchange (FX) payments

As FIs face both an increase in cross-border transactions and a continued drive for efficiency, they are under pressure to develop greater capabilities to support their clients' intra-regional and global growth more cost-effectively. These challenges would be significant at any time, and the advent of Basel III is making them even more complex.

While global banks have invested significant sums in their FX and cash management platforms to meet the increasingly sophisticated demands of their customers, local FIs face significant cost pressures in offering similar solutions, particularly if cross-border FX capabilities are not part of their core offering. The costs associated with building and rolling out integrated FX and payment platforms can be high, and they need further resources to comply with new regulatory requirements, navigate clearing and settlement systems, and offer more language capabilities. Yet, without these enhancements, the ability of local FIs to retain their business, let alone target new flows and opportunities, can be limited.

FIs can still target market-share opportunities in this environment through an assessment of business operations and future plans. By addressing these obstacles with the help of global banking partners, Indonesian FIs can focus on building a stronger relationship with their clients, increase business performance and improve their market share. They can further differentiate their services through counterparty stability, access to global clearing networks, superior client service models, a wider range of currencies, and more.

In a market that continues to grow rapidly, Indonesian FIs can leverage new tools and expertise to optimise their business by working with a global bank, and tapping into new products and solutions as well as best practices that can further enhance their business competitiveness

Michael Sugirin, Head of Treasury Services, Indonesia

As Indonesian companies look further afield to sell their products and to source imports, and as they then require services support for international growth and cross-border transactions, domestic FIs need to adapt and be in a position to make their clients' international journey smooth and cost-effective. FIs face the challenge of balancing the cost and complexity of opening a multitude of new 'nostro' accounts and developing technology with the opportunities of business from key corporate clients as well as from consumers.

An alternative solution for FIs is to establish a relationship with a global bank that can assist with management of cross-border flows and provide services that streamline processes, reduce overheads and extend services to more markets for their clients. For example, local FIs can leverage the existing technology of a global bank and quickly offer a USD payments service, which provides the ability to convert single-currency US dollar payment instructions into payments in the currency of the beneficiary location, based on agreed parameters. A company can use this type of service to send a payment from their US dollar account to their counterparty in Germany, for example, with the global bank converting the payment into euros on behalf of the local FI. Converting what would be a USD payment into a local currency payment offers an opportunity to reduce the payment delivery time and generate an additional stream of revenue from the foreign exchange, with no requirement to amend existing SWIFT instructions and with use of existing accounts. Overall lower costs for a majority of transactions – and especially those under US$50,000 – makes such a service very attractive.

In selecting which global bank to use for this service, a key consideration is which bank the Indonesian FI uses for dollar clearing, since going to another bank would require them to open another nostro account and maintain additional balances at the second bank. While many large Indonesian FIs have already established such a facility, those banks that have not can also determine whether they will benefit from it by analysing whether their corporate or consumer clients are starting to ask for payments in local currencies, and assessing their readiness to provide the service if the demand continues to grow.

Even though imports and exports may have slowed, the continuing growth in demand for foreign currency payments – whether they are outbound payments for goods imported from overseas or expenses such as payment of school fees for students studying abroad, or inbound payments such as remittances from foreign domestic workers and for exports – there will always be a need for payments outside of Indonesia.

Anti-money laundering

AML is an ongoing concern for FIs in Indonesia as well as in other countries, as regulators in Indonesia continue to strengthen existing requirements and as the impact of the increasing focus by regulators in the West also continues to affect FIs in Asian markets. As such, FIs in Indonesia need to ensure they continue to meet the requirements of their regulators and counterparties.

While Indonesian banks are indeed strengthening their systems and processes, and operations staff now clearly understand the rules and look out for anomalies, domestic FIs are also looking for sharing of knowledge and best practices so that they can strengthen risk control in the back office even further. Indonesian FIs can leverage the experience and expertise that global banks have developed in markets around the world through knowledge-sharing and by obtaining information about regulatory updates in other markets that may affect them in Indonesia as well, whether it is for OFAC or other requirements. To ensure they keep up with global developments and implement consistent practices across their institutions, Indonesian FIs can engage their global bank to gain knowledge from other markets, obtain information about leading-edge practices in staying abreast of compliance updates, and learn how to manage the back office better to ensure compliance.

Conclusion

In a market that continues to grow rapidly despite occasional setbacks, Indonesian FIs can leverage new tools and expertise to optimise their business by working with a global bank, and tapping into new products and solutions, as well as best practices that can further enhance their business competitiveness.

J.P.Morgan

Michael Sugirin
Head of Treasury Services, Indonesia
E: michael.sugirin@jpmchase.com
T: +62 21 5291 8551
www.jpmorgan.com/ts