

Validation Report
June 2021

Indonesia: Financial Market Development and Inclusion Program

Reference Number: PVR-772
Project Numbers: 48207-001, 48207-002, 48207-004
Loan Numbers: 3274, 3541, 3779

Independent
Evaluation  ADB

Raising development impact through evaluation

ABBREVIATIONS

| | |
|-------|---|
| ADB | – Asian Development Bank |
| ASEAN | – Association of Southeast Asian Nations |
| bps | – basis points |
| DMF | – design and monitoring framework |
| FPA | – Fiscal Policy Agency |
| GDP | – gross domestic product |
| IFSB | – Islamic Financial Services Board |
| MOF | – Ministry of Finance |
| OJK | – Otoritas Jasa Keuangan (Financial Services Authority) |
| PATA | – policy and advisory technical assistance |
| PCR | – project completion report |
| TA | – technical assistance |

NOTE

In this report, “\$” refers to United States dollars.

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|-------------------------|--|
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| Director | Nathan Subramaniam, Sector and Project Division (IESP) |
| Team Leader | Paolo Obias, Principal Evaluation Specialist (IESP) |

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PROGRAM BASIC DATA

| | | | | | |
|--------------------------------------|---|--------------------------------------|---------------------------------|-------------------------------|--------|
| Program numbers | 48207-001, 48207-002, and 48207-004 | PCR circulation date | 3 Dec 2020 | | |
| Loan numbers | 3274, 3541, and 3779 | PCR validation date | Jun 2021 | | |
| Program name | Financial Market Development and Inclusion Program | | | | |
| Sector and subsector | Finance | Finance sector development | | | |
| Strategic agenda | Environmentally sustainable growth Inclusive economic growth Regional integration | | | | |
| Safeguard categories | Environment | | C | | |
| | Involuntary resettlement | | C | | |
| | Indigenous peoples | | C | | |
| Country | Republic of Indonesia | | Approved (\$ million) | Actual (\$ million) | |
| ADB financing (\$ million) | ADF: 0.00 | Total project costs | 1,300.00 | 1,300.00 | |
| | OCR: 1,300.00 | Loan | | | |
| | | 3274 | | 400.00 | 400.00 |
| | | 3541 | | 400.00 | 400.00 |
| | | 3779 | | 500.00 | 500.00 |
| | | Borrower | | 0.00 | 0.00 |
| | Beneficiaries | | 0.00 | 0.00 | |
| | Others | | 0.00 | 0.00 | |
| Cofinancier | – | Total cofinancing | 0.00 | 0.00 | |
| Approval date | | Effectiveness date | | | |
| 3274 | 1 Sep 2015 | 3274 | 29 Dec 2015 | 27 Oct 2015 | |
| 3541 | 28 Jun 2017 | 3541 | 16 Oct 2017 | 7 Sep 2017 | |
| 3779 | 28 Mar 2019 | 3779 | 1 Aug 2019 | 27 Jun 2019 | |
| Signing date | | Loan closing date | | | |
| 3274 | 30 Sep 2015 | 3274 | 30 Jun 2016 | 3 Feb 2016 | |
| 3541 | 18 Jul 2017 | 3541 | 31 Mar 2018 | 15 Nov 2017 | |
| 3779 | 3 May 2019 | 3779 | 31 Mar 2020 | 1 Jul 2019 | |
| | | Financial closing date | | | |
| | | 3274 | | 3 Feb 2016 | |
| | | 3541 | | 15 Nov 2017 | |
| | | 3779 | | 1 Jul 2019 | |
| Project officers | | Location | From | To | |
| | S. Ismail P. Jayawardana | ADB headquarters ADB headquarters | 4 Sep 2015 27 Apr 2018 | 29 Jul 2019 29 Jul 2019 | |
| IED review | | | | | |
| Director | N. Subramaniam, IESP | | | | |
| Team leader | P. Obias, Principal Evaluation Specialist, IESP* | | | | |

ADB = Asian Development Bank, ADF = Asian Development Fund, IED = Independent Evaluation Department, IESP = Sector and Project Division, OCR = ordinary capital resources, PCR = project completion report.

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I. PROJECT DESCRIPTION

A. Rationale

1. Indonesia dealt with the twin problems of insufficient growth and rising household inequality. The economy underwent a prolonged economic slowdown where the gross domestic product (GDP) declined from 6.2% in 2010 to 4.9% in 2015. The decline was mainly due to the end of the commodity boom and tightening of macroeconomic policies to lower inflation, curb the current account deficit, and stabilize the rupiah exchange rate.¹ Against this backdrop of economic slowdown, the Gini index rose from 37.9 in 2010 to 41.0 in 2015. In response to these twin problems, the government's National Medium-Term Development Plan (RPJMN) for 2015–2019 sought to achieve growth with equity and targeted a GDP growth rate of 8%, reduction of the Gini index to 36.0, and decline in the poverty rate to 7%–8% by 2019.²

2. Beset with inadequate growth and inequality, the government recognized the critical role of a deep, liquid, and efficient financial market in promoting financial stability, new sources of growth, and financial inclusion. In line with this, the government targeted the finance sector to grow 10.4% year-on-year by 2019, from 8.2% in 2014, and to provide access to finance to 25% of the poorest 40% of the population by 2019.

3. The government recognized the binding constraints in achieving a stable, developed, and inclusive finance sector. These constraints consisted of (i) incomplete regulatory framework and institutional coordination which posed risks to the finance sector's stability, (ii) limited diversity of saving and capital market instruments and policies that foster growth in markets for these instruments, and (iii) low access to financial services for the poor. Despite the establishment of the Otoritas Jasa Keuangan (OJK) or Financial Services Authority, there were gaps or inconsistencies in its operations and policies in conjunction with other agencies. An integrated implementation of OJK's master plan was required to avoid distortion and regulatory arbitrage, and an integrated supervision was also needed to better supervise financial conglomerates. The finance sector was dominated by banks, and the equity market was below 50% of GDP in 2014. In contrast, comparators from the Association of Southeast Asian Nations (ASEAN), such as Malaysia, the Philippines, Singapore, and Thailand reported market capitalization of over 90% of their respective GDPs. The corporate bond market was only 2% of GDP, compared with the East Asia's average of 21%. Financial exclusion was a problem since only 21.9% of the poorest 40% had savings in a financial institution. Only 34% of women had access to financial services, and based on a survey, financial literacy among women was low at only 26% in 2016.

4. The Financial Market Development and Inclusion Program was formulated to support the priorities of the government and the OJK to further develop and make the finance sector more inclusive by strengthening the regulatory structure for financial stability, deepening the financial market, and enhancing financial inclusion. This program comprised three subprograms. Subprogram 1 focused on institutionalizing OJK as an integrated and independent financial services regulator and implementing best practices in promoting capital market development.³ Subprogram 2 supported the development of OJK's consolidated finance sector master plan,

¹ Bank of Indonesia increased BI rates to 7.75% in November 2014 after inflation peaked to above 8%. The BI rate is the base rate (policy rate) which is used by the central bank of Indonesia to shape the monetary policy.

² Government of Indonesia. 2015. *National Medium-Term Development Plan: RPJMN, 2015–2019*. Jakarta.

³ ADB. 2015. *Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Loan for Subprogram 1 to the Republic of Indonesia for the Financial Market Development and Inclusion Program*. Manila.

which focused on making the sector stable, inclusive, and contributive to the economy.⁴ Subprogram 3 focused on implementing the master plan, expanding capital markets products and services, and advancing financial inclusion using financial technology.⁵

B. Expected Impact, Outcome, and Outputs

5. The program's expected impact was increased annual growth of the finance sector in alignment with the National Medium-Term Development Plan, 2015–2019. Its envisaged outcome was increased development and inclusiveness of the finance sector. The program's targeted outputs were (i) strengthened regulatory structure for financial stability, (ii) deepened financial market, and (iii) enhanced access to financial services.

C. Provision of Inputs

6. The programmatic approach comprised three subprograms. Subprogram 1 was approved for \$400 million in September 2015 and became effective in October 2015. Subprogram 2 was approved for \$400 million in June 2017 and became effective in September 2017. Subprogram 3 was approved for \$500 million in March 2019 and became effective in June 2019.

7. The program implementation period, which included the realization of reform actions prior to loan approval, was from January 2013 to January 2019. All three subprograms were closed before the expected closing dates. Subprogram 1 was implemented from January 2013 to June 2015 and closed 4.9 months ahead of the expected closing date. Subprogram 2 was implemented from July 2015 to March 2017 and closed 4.5 months ahead of the expected closing date. Subprogram 3 covered April 2017 to January 2019 and was closed 9.1 months earlier than the expected closing date. The loans for all subprograms were released in single disbursements within 1 week after loan effectivity.

8. The program was classified as category C for impacts on the environment, involuntary resettlement, and indigenous peoples. Subprogram 1 had no gender elements, but subprograms 2 and 3 were classified as effective gender mainstreaming programs as these included financial literacy initiatives for women.

9. Subprograms 2 and 3 were supported by a policy and advisory technical assistance (PATA).⁶ The PATA in the amount of \$1.5 million supported the outputs for the policy actions across the three subprograms. It covered assistance for financial stability, financial deepening and inclusion, and was utilized to support the completion of reforms in subprograms 2 and 3.

D. Implementation Arrangements

10. As envisaged in the design, the Fiscal Policy Agency (FPA) in the Ministry of Finance (MOF) was the executing agency of the program with the OJK, represented by the International Department, as the implementing agency. Other agencies involved were the Bank of Indonesia and the Securities Investor Protector Fund. The joint MOF–OJK committee chaired by the FPA

⁴ ADB. 2017. *Report and Recommendation of the President to the Board of Directors: Proposed Policy-Based Loan for Subprogram 2 and Technical Assistance Grant to the Republic of Indonesia for the Financial Market Development and Inclusion Program*. Manila.

⁵ ADB. 2019. *Report and Recommendation of the President to the Board of Directors: Proposed Policy-Based Loan for Subprogram 3 to the Republic of Indonesia for the Financial Market Development and Inclusion Program*. Manila.

⁶ ADB. 2015. *Technical Assistance to the Republic of Indonesia for Enhancing the Regulatory Framework of Financial Sector Development and Oversight*. Manila.

discussed the reforms in the policy matrix and the finance sector in general. The implementation arrangements were adequate in monitoring the reforms and delivering the expected outputs.

11. Subprogram 1 had 23 policy actions, of which 12 were policy triggers. These were fully accomplished. Subprogram 2 had 25 policy actions, comprising 9 policy triggers and 16 policy milestones, all of which were accomplished. Key policy triggers were the regulations to support the Law on Prevention and Resolution of Financial System Crisis and measures to advance the financial inclusion agenda. Subprogram 3 had 23 policy actions consisting of 13 triggers and 10 policy milestones, all of which were fully accomplished. Key policy triggers included an enabling environment for issuance of municipal bonds, operationalization of the National Council for Financial Inclusion, and OJK's implementation of priority reform actions in the consolidated finance sector master plan. There were 45 loan covenants for the three subprograms, all of which were complied with.

12. The PATA supported activities, such as engagement of experts that provided policy advice, procurement of equipment for operations, capacity building through workshops, and awareness-raising through an international conference that aimed to examine financial stability issues from a regional perspective.

II. EVALUATION OF PERFORMANCE AND RATINGS

A. Relevance of Design and Formulation

13. The project completion report (PCR) rated the program relevant at appraisal and at completion.⁷ It attributed this rating to the program design that embedded the policy matrix within the government's policy decision-making process. The loan proceeds provided the incentives and enabled the necessary reforms in the finance sector with TA support on capacity building of the government and the OJK. The program's outputs strengthened the regulatory structure for financial stability and deepened the financial market, particularly the capital market. The consolidated finance sector plan developed and supported by ADB during the program ensured that the reforms were appropriately supported by the OJK's reform agenda. Financial inclusion was enhanced through broader access to finance, improvement in financial literacy, and strengthened consumer protection.

14. The program was consistent with ADB's country partnership strategy for 2016–2019 that supported policy reforms for strengthening the enabling environment for inclusive growth.⁸ It was also aligned with the operational priorities of ADB's Strategy 2030 on addressing the remaining poverty and inequality, and accelerating progress on gender equality. The institutionalization of OJK was in line with Strategy 2030's operational priority on strengthening governance. The sequential approach of the reforms to institutionalize OJK as an integrated regulator, followed by development in the capital market before advancing financial inclusion and literacy initiatives, were suitable in the country's context.

15. This validation notes that the programmatic approach was appropriate to chronologically sequence the package of reforms in a coherent and comprehensive framework. The subprograms and corresponding policy actions were generally well sequenced. The results chain in the design and monitoring framework (DMF) established the linkages from policy actions to outputs—

⁷ ADB. 2020. *Completion Report: Financial Market Development and Inclusion Program in Indonesia*. Manila.

⁸ ADB. 2016. *Country Partnership Strategy: Indonesia, 2016–2019—Towards a Higher, More Inclusive and Sustainable Growth Path*. Manila.

covering regulatory structure for financial stability, diversification of financial instrument and market deepening, and inclusion—to the envisaged outcome of increased development and inclusiveness of the finance sector. Majority of the policy actions were of good quality. Of the 71 policy actions for the three subprograms, 42 (59%) were actions that can be considered to have long-lasting changes on the policy and institutional environment. For example, these include the ratification and implementation of the Law on Prevention and Resolution of Financial System Crisis, digital finance regulations to promote consumer protection, and online e-modules to increase access to financial literacy. Thirty-seven percent of the policy actions were of medium-depth policy actions that had immediate effects but needed to be followed through to achieve long-lasting changes. Only 4% of the policy actions can be considered low in depth for not bringing about any significant policy or institutional changes. The indicators in the DMF were appropriate and logically linked to the output and outcome statements. This validation assesses the program relevant.

B. Effectiveness in Achieving Project Outcome and Outputs

16. The PCR rated the program effective based on the achievement of the outcome and output targets. In terms of the outcome targets, the three performance targets were exceeded during subprogram 1. By the end of 2017, the size of the finance sector grew by about 14% of GDP, which exceeded the target of 12%. Access to financial services of the poorest 40% improved from 22% in 2014 to 37% in 2017, exceeding the target of 25%. Based on the Global Findex Database, Indonesia's overall financial inclusion level was 49% in 2017, which was a significant improvement from 36% in 2014. In the same manner, the 5-year credit default swap (CDS) spread which was used as a proxy measure for financial stability declined by more than 70 basis points (bps) by end of 2017. This exceeded the target of 20 bps reduction. The three performance indicators were exceeded during subprogram 1 and were consequently revised upwards for 2020 under subprogram 3. Of the three revised targets, two were met and one was not met. Access of the poorest 40% to financial services increased to 50.2%, surpassing the revised target of 40.0%. The 5-year CDS spreads indicator declined by about 100 bps at the end of 2019, exceeding the target of 30 bps. The size of the finance sector shrunk from 117% of GDP to 113% by end of 2018, which did not meet the target of 20% increase in the share to GDP. In terms of the outputs, all output performance targets were achieved, except for the target on the submission of the revised capital market law to parliament. The Law on Prevention and Resolution of the Financial System Crisis, which provided OJK with legal immunity, was given higher priority during the negotiation between the government and the parliament.

17. This validation confirms that the envisaged outcome of increase in development and inclusiveness of the finance sector was achieved. The original outcome targets were all met and only one of the revised (and increased) targets during subprogram 3 was not met. This represented 83% achievement of targets, which indicated achievement of envisaged outcome. This validation notes that the outputs undoubtedly contributed to the achievement of the envisaged outcome. However, due to the broad and high-level targets for outcome, it is difficult to attribute the achievement of the outcome solely to the outputs delivered by the program. Other factors such as regulatory and policy measures beyond the program affect the size of the finance sector, financial stability, and the extent of financial inclusion.

18. Of the three outputs, two were fully realized and one was partially achieved. Subprogram 1 under the output on strengthened regulatory structure for financial stability (output 1) met three of the four targets. The targets met were OJK's (i) implementation of the roadmap of priority reforms with specific targets and monitoring mechanism, (ii) implementation of cross sector consolidated supervision, and (iii) completion and implementation of an information and

communication technology system to support integrated reporting, licensing, and supervision. The target that was not achieved pertained to the submission to parliament of the revised law on capital market. Instead, the parliament prioritized the Law on Prevention and Resolution of Financial System Crisis. Subprogram 2 continued the focus on the implementation of the master plan and integrated supervision. The two targets under the subprogram were met: (i) OJK implemented 90% of the priority reforms in the consolidated finance sector masterplan, which exceeded the target of at least 50%; and (ii) OJK's integrated supervision became fully operational with regular on-site examinations of conglomerates conducted. Likewise, the two targets for subprogram 3 were met. First, OJK implemented 90% of the priority reform actions and 83% of other actions in the consolidated finance sector master plan. Second, the regulation to regulate financial holding companies was drafted by OJK as planned.

19. On the deepening of the financial market (output 2), all the targets in the three subprograms were met. Under subprogram 1, the capital market was diversified to include private equity funds, mortgage-backed securities, exchange-traded funds, derivatives products, and Islamic capital market instruments. By 2015, OJK implemented 50% of the Islamic Financial Services Board (IFSB) standards as planned. Subprogram 2 continued the focus on diversifying the capital market through the development of Islamic finance. The tax neutrality framework for Islamic capital market product was developed and a decision was issued. This provided equal tax treatment for Islamic capital market instruments and conventional capital market products. In terms of the monitoring and evaluation system of the National Health Insurance, the government dashboard monitoring and evaluation system to monitor the progress of National Health Insurance was made available online. Under subprogram 3, OJK met the target of implementing all IFSB standards for capital market and Takaful, and 67% of IFSB standards for banking. These were key actions that were achieved on the adoption of international standards. In addition, the municipal bond financing plan and detailed list of projects were approved by the local government of Central Java as planned.

20. On enhancing access to financial services (output 3), all nine targets across the three subprograms were likewise achieved. Under subprogram 1, the international learning center for microfinance was established. The function of the learning center was subsequently folded into OJK Infinity which combined the function of promoting financial inclusion and the function of an innovation center for financial technology (fintech). OJK conducted financial literacy programs in at least 30 cities and 10 outreach programs. These continued into subprogram 2, which built on reforms to improve financial inclusion of women. Under subprogram 2, OJK Infinity undertook regular training programs for microfinance and the general public. The target of two training programs was achieved. The envisaged National Council for Financial Inclusion was established. OJK completed the financial literacy survey by increasing respondents to 9,680 including women (49%) and analysis of sex-disaggregated data. It implemented five outreach programs on financial literacy, including focus group discussions for women. OJK assessed the consumer protection framework for government-to-people initiatives and approved the expansion of branchless banking initiative. Under subprogram 3, the actions for financial inclusion were pushed further. The National Council for Financial Inclusion became fully operational with seven working groups, including financial literacy and consumer protection. The target of implementing 40 financial literacy programs was met. The branchless banking initiative launched by OJK to promote financial inclusion expanded significantly with 29 banks and 800,000 participating agents. This was instrumental in providing access to finance for the poorest 40% of the population. This was also an important development for women's financial inclusion as women have greater mobility constraints.

21. Of the 21 output targets of the program, only one was not achieved, which means a 95% achievement rate. In terms of the outcome targets, all the original outcome targets were met and only one of the revised targets was not met. Most of the outputs were delivered as well as the envisaged program outcome. This validation assesses the program effective in achieving the intended outcome.

C. Efficiency of Resource Use

22. The PCR rated the program highly efficient. It indicated that the outcome was achieved within the planned implementation period. The three subprograms were declared effective prior to the stated date in the loan agreement. Disbursements followed quickly after the declaration of effectiveness. There were no extensions on implementation and all three subprograms were closed ahead of schedule. Some of the key benefits of the program were reduction in the cost of borrowing in bond markets, increase in issuances and investments in the Islamic capital market through tax neutrality, efficiency gains through the branchless banking initiative, and degree of financial inclusion.

23. This validation notes that the processes of the three subprograms are highly efficient as demonstrated by the early effectiveness of the loans, quick disbursements, and closing of the loans ahead of schedule. There was no need for any extension as deliverables were produced on time. The borrower achieved substantive reform actions prior to the subprogram loan approvals. The economic benefits were brought about by strengthening of the regulatory structure for financial stability, deepening of the financial market, and greater financial inclusion. In view of the efficient processes and the benefits gained by the program, this validation assesses the program highly efficient.

D. Preliminary Assessment of Sustainability

24. The PCR rated the program likely sustainable, especially the output on enhancing access to finance. The National Strategy on Financial Inclusion, which was successfully implemented, and the National Financial Literacy Strategy will promote sustained access to financial services and integrate the unbanked in the formal financial system. The National Council for Financial Inclusion, as focal point, will sustain the government's inclusion initiatives beyond the program implementation period. In December 2020, ADB approved a financial inclusion program to further deepen access through innovative approaches.⁹

25. This validation considers the program outputs likely sustainable as well. On the regulatory structure for financial stability, the Law on Prevention and Resolution of Financial System Crisis enacted in 2016 was a significant landmark for financial stability. OJK became fiscally autonomous and launched the consolidated finance sector master plan, which prescribed the key finance sector reforms. These legal, institutional, and policy changes have long-lasting effects on the sector and cannot be easily reversed. On deepening of the financial market, the capital market was diversified; tax neutrality decision for Islamic capital market products was issued; IFSB standards covering banking, capital market, and insurance were implemented; and the problem of overlapping audit requirements was resolved. These policy and institutional changes are likely to be sustained beyond the program period as these were firmly established in the finance system. The three program outputs are likely to be sustained beyond the program period. Also, the post-

⁹ ADB. 2020. *Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Loan for Subprogram 1 to the Republic of Indonesia for Promoting Innovative Financial Inclusion Program*. Manila.

program partnership framework will contribute further to the sustainability of the program outcome. The framework provided for a structured dialogue between ADB, the government, and OJK over the medium-term in advancing finance sector reforms. This validation assesses the program likely sustainable.

III. OTHER PERFORMANCE ASSESSMENTS

A. Preliminary Assessment of Development Impact

26. The PCR rated the program's development impact satisfactory, based on the cumulative reforms that produced high-level impacts in two of the three outputs throughout the three subprograms. In particular, the output on financial stability, mainly by institutionalizing OJK as an integrated regulator with fiscal autonomy and legal immunity, was essential for an independent regulatory agency. Also, OJK developed and implemented its first consolidated master plan. The output on inclusive finance broadened access to finance, financial literacy, and strengthened consumer protection. Key reforms included the establishment of the National Council for Financial Inclusion and launching the expansion of branchless banking initiatives. Women's access to bank accounts rose from 38% in 2014 to 51% in 2017. The PCR acknowledged that the output on deepening the finance sector had modest impacts. Although progress was realized in the adoption of international standards, the size of the government and corporate bond market still lagged behind comparator countries in ASEAN. The PCR indicated that program impact assessments of the three subprograms showed net benefit to the economy, which included reduced cost of borrowing in bond markets, increased financial inclusion, and increased Islamic finance investment resulting from tax neutrality measures.

27. This validation notes that the program's expected impact, as stated at the program design stage and maintained in the DMF (i.e., increased annual growth rate of the finance sector), was both narrowly focused and somewhat repeated one of the program's outcome targets, which was to increase the size of finance sector as a percentage of GDP. The implementation of the consolidated master plan was an important milestone for OJK as it covered reforms on banking, capital market, and nonbank financial institutions, and crosscutting themes such as financial inclusion and consumer protection. The Law on Prevention and Resolution of Financial System Crisis was an important piece of legislation that provided legal immunity to OJK in performing its duties in good faith and in becoming fiscally autonomous. The plan to submit to parliament a revised law on capital market did not materialize because of other legislative priorities of the parliament. However, the capital market was diversified consisting of equities, bonds, mutual funds, exchange-traded funds, *sukuk*,¹⁰ mortgage-backed securities, and private equity funds. Institutional mechanisms were set in place to advance the financial inclusion agenda. The international learning center for microfinance and the National Council for Financial Inclusion were established. Also, the initiatives on branchless banking initiated by OJK had a significant impact on financial inclusion, as indicated by the increase in the number of account holders and women's access to finance from 38% in 2015 to 51% in 2017.¹¹ This validation assesses the development impact of the program satisfactory.

B. Performance of the Borrower and Executing Agency

28. The PCR rated the performance of FPA at the MOF as executing agency and OJK as implementing agency satisfactory. Both agencies regularly updated ADB on the progress of

¹⁰ *Sukuk* is a capital-raising instrument that provides undivided ownership over underlying assets.

¹¹ World Bank. *The Global Findex Database 2017*. Washington, DC.

reforms and challenges. The borrower was able to complete key prior reform actions before each of the three subprograms was approved. These were accomplished in line with the original schedule set in 2015, during the approval of subprogram 1. The FPA and OJK demonstrated ownership of the program with ADB having access to the head of FPA and chairman of OJK for high-level policy dialogue. The steering committee chaired by the deputy minister of MOF (head of FPA) effectively coordinated the reforms within the government and OJK. The Center for Financial Sector Policies that was set up within MOF monitored the implementation of the policy actions in coordination with OJK. The government met the conditions of the loan and completed the program ahead of closing schedule. This validation assesses the performance of the executing agency and implementing agency satisfactory.

C. Performance of the Asian Development Bank and Cofinanciers

29. The PCR rated the performance of ADB satisfactory. ADB had adequate institutional experience and knowledge of the finance sector to help address key issues and constraints. The lessons learned from the previous finance sector program were incorporated in the program design. The outposting of the mission leader in the resident mission in 2017 helped intensify engagement with the government and OJK in policy dialogue and advisory support in technical areas such as Islamic finance, corporate governance standards, and investor protection. ADB provided the necessary support for the policy reforms outlined in the policy matrix such as the OJK's consolidated master plan, the information technology system improvement, implementation of IFSB standards, and e-modules for financial literacy. ADB was responsive to the needs of the government in addressing the identified sector issues and constraints. There were no delays in processing. ADB also coordinated with development partners on the reform program. This validation assesses the performance of ADB satisfactory.

D. Others

30. The program did not encounter governance issues during implementation. There were no reports or evidence of corrupt, fraudulent, or coercive practices and as such, no audits or investigations were launched.

IV. OVERALL ASSESSMENT, LESSONS, AND RECOMMENDATIONS

A. Overall Assessment and Ratings

31. The PCR rated the program successful. This validation assesses the program relevant, effective, highly efficient, and likely sustainable. The program was relevant as it was in line with government's priorities and supported reform efforts in financial market development, including financial inclusion. It was effective in achieving its intended outcome of increasing the development and inclusiveness of the finance sector. It was highly efficient in implementing the program and delivering the outputs and outcome. The program is likely sustainable as its outputs are likely to be sustained beyond the program period in view of the institutional and legal reforms that have been set in place and follow-on dialogue, and the activities that have taken place in line with the post-program partnership framework. Overall, this validation assesses the program successful.

Overall Ratings

| Validation Criteria | PCR | IED Review | Reason for Disagreement and/or Comments |
|----------------------------------|--------------------|--------------------|---|
| Relevance | Relevant | Relevant | |
| Effectiveness | Effective | Effective | |
| Efficiency | Highly efficient | Highly efficient | |
| Sustainability | Likely sustainable | Likely sustainable | |
| Overall Assessment | Successful | Successful | |
| Preliminary assessment of impact | Satisfactory | Satisfactory | |
| Borrower and executing agency | Satisfactory | Satisfactory | |
| Performance of ADB | Satisfactory | Satisfactory | |
| Quality of PCR | | Satisfactory | Para. 37. |

ADB = Asian Development Bank, IED = Independent Evaluation Department, PCR = project completion report.
Source: ADB (IED).

B. Lessons

32. This validation notes that the lessons presented in the PCR are suitable and useful. First, establishing an effective integrated finance sector regulator, such as the OJK, requires appropriate sequencing of actions, starting with legislation and measures to ensure legal and fiscal autonomy, as well as legal immunity for staff. The TA support is necessary to help the government accomplish their reform agenda. Second, financial stability and capital market development need to be accompanied by reforms to increase access to financial services of the poor so as to maximize economic impact. The PCR noted that it is important to pair efforts to increase financial inclusion with reforms in financial literacy and consumer protection. Third, a crosscutting finance sector program, covering financial stability, capital market development, and financial inclusion, is viable only in the early stages of finance sector development. Over time, a dedicated program focusing on one subsector or theme is preferable. Fourth, predicating a program on the passage of a law should be minimized unless there is a strong ownership to pass the law both by the executive and legislative branches of the government. The reform agenda could have been served better with a dedicated TA to identify capital market constraints, followed by advisory support to draft revisions to existing law(s). Lastly, national finance sector development could have included international and regional considerations since Indonesia is a member of G20 and ASEAN, which increasingly require harmonization in finance sector management.

33. This validation reconfirms the lesson about the importance of a comprehensive strategic framework that broadens and deepens financial inclusion based on robust diagnostics and analytical work. The rationale for reform and policy actions are to be drawn from these diagnostics, and actions are prioritized and sequenced in addressing the constraints and bottlenecks. Regulatory constraints, institutional capacity limitations, deficiencies in technology infrastructure, and extent of financial literacy need to be clearly identified and assessed based on the analytical work. Related to the first lesson outlined in the PCR on the importance of TA and resident consultant support, this validation notes that the continuous longer-term involvement of the same mission leader and other qualified ADB staff from the design stage until the end of implementation of the three subprograms is important to the success of this program. Familiarity with local

institutional challenges and personnel in the government is important for a complex reform program such as this one to achieve progress.

34. Another lesson is on the quality and timing of the TA in supporting policy-based loans for policy reforms. It is important that the TA is appropriately designed to support the delivery of expected outputs and that it is implemented in a timely manner. The program demonstrated the role of a well-designed TA in supporting completion of reforms across the three subprograms and building capacity of the implementing agency. It is also essential that the timing of activities is aligned with the sequencing of policy actions so as not to undermine the achievement of outputs.

C. Recommendations for Follow-Up

35. The recommendations of the PCR for post-program follow-up actions are sound and appropriate. First, focused efforts are needed to reach more of the unbanked and underbanked populations through innovative approaches including use of fintech. Second, the policy matrix for future programs should focus on high impact milestone reforms since quality is more important than quantity, and ADB has limited staff and TA resources for dialogue and issues resolution. Third, ADB should engage stakeholders more widely particularly those involved in financial inclusion. Lastly, programs should minimize reforms that require changes in legislation.

V. OTHER CONSIDERATIONS AND FOLLOW-UP

A. Monitoring and Reporting

36. The MOF's FPA in coordination with the OJK's International Department monitored the implementation of the policy actions under the policy matrix. They also reported on the policy reforms in the matrix and the indicators in the DMF. Monitoring of the program was adequate and satisfactory. The post-program partnership framework and follow-on programs in the sector will provide a platform for ADB and the government to dialogue and monitor reform progress in the finance sector.

B. Comments on Project Completion Report Quality

37. The quality of the PCR is assessed satisfactory. The analysis and discussions were well presented, especially the tables outlining the progression in output achievements under the three subprograms. The PCR is prepared with a good understanding of the broad finance sector status and issues in Indonesia. The ratings were adequately substantiated with evidence. The lessons were drawn from the findings, and the recommendations were sound. The DMF clearly presented the achievements vis-à-vis the targets. The achievements on gender-related targets and policy actions were informative.

C. Data Sources for Validation

38. The sources for this validation were the reports and recommendations of the President on the three subprograms and their linked documents, the PCR, back-to-office reports, TA report, TA completion report, and minutes of management review meetings.

D. Recommendation for Independent Evaluation Department Follow-Up

39. None.