

The Role of Islamic Microfinance to Support the Growth of Small – Medium Enterprises: Case Study of SMEs in Jakarta, Depok, Bogor and Tangerang

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Abstract: The role of Small and Medium Enterprises (SMEs) become prominent in the economic development of a country. However, despite of their importance, SMEs have less access to formal source of external finance. The rise of Islamic microfinance is expected to overcome the financial constraint facing by SMEs. Accordingly, this study aims to investigate the role of islamic microfinance on the growth of small -medium enterprises. The sample comprised of 160 customers of four islamic microfinance institution located in Jakarta, Bogor, Depok, dan Tangerang. The regresion results empirically show that islamic microfinance variables used in this research are positively related with the growth of small – medium enterprises in the samples. Trainings and loan frequency are significant to affect the growth of SMEs.

1 INTRODUCTION

Globally, SMEs have proven to contribute significantly to GDP and also to employment (EdinburghGroup,2014). As a developing country, MSMEs certainly have a very important role for the Indonesian economy (Sarwono,2015). In the last five years, the contribution of the MSME sector to Indonesia's Gross Domestic Product increased from 57.84% to 60.34% (Kemenperin,2018).

However, SMEs globally have a major problem that is the limitations of capital (Christopher,2010). Lack of access to financial support has been identified as one of the main problems for the growth of SMEs globally, also in Indonesia (Sarwono,2015). There are about 60-70% of MSMEs in Indonesia have not been able to get access to financing or credit from banks (Sarwono,2015). This is based on the fact that there are still few banks that can reach the remote areas of UMKM throughout Indonesia. In addition, there are also administrative constraints of MSMEs that do not meet the requirements. Therefore, the existence of Micro Finance Institution and Sharia Micro Finance Institution in Indonesia is a solution to reduce the problem of capital limitations to MSMEs. The success of microfinance institutions has been proven and successful in Muslim-majority countries such as

Indonesia, Bangladesh, Pakistan, Turkey and others (Rokhman,2013). However, this product does not meet the needs of all Muslim clients.

Today, sharia financial institutions are a growing industry worldwide. This is because Islamic financial institutions have their own attractiveness that is the practice in accordance with Islamic principles and theories (Amin et al.,2011). In Indonesia, the growth of sharia financial institutions is an interesting phenomenon. Not only sharia banking, shariah micro-finance institutions are also growing and increasing in number. Referring to the market potential and the important role of of Islamic Microfinance Institution, therefore,

Research from Rokhman (2013) showed that microfinance has an important role in increasing income levels, children's education, and business progress. However, Babajide (2012) revealed an inverse result that microfinance in Nigeria did not increase the growth of MSMEs. Hence, this study aims to investage whether islamic financing can support MSMEs' growth.

2 LITERATURE REVIEW

In general, Islam supports the rotation or transfer of wealth from surplus units to deficit units that will assist in the development of socio-economic welfare of the needy (Ali et al.,2015). Financing in Islam has two main goals. First, financing in Islam has the goal of channelling resources and wealth from surplus units to deficit units. Second, to meet human needs and enable Muslims to improve their welfare (Kahf and Khan,1992). Basically, Islam does not encourage someone to carry debt. Every debt must be based on real needs, therefore as much as possible Islam regulates its people to have no debt. (Amin et al.,2011).

A numerous of empirical studies has been conducted to investigate the role of microfinance in supporting the growth of SMEs. Adnan & Ajija (2015) investigate the effectiveness of *Baitul Maal wat Tamwil* (BMT) in reducing poverty. The empirical results show that financing from BMT is significant in reducing poverty. The findings confirm that most respondents experiencing an increase in the level of income after receiving financing from BMT. Other BMT's products, especially mudharabah, have positive contribution to empower the poor in various productive programs and also able to reduce the level as well as the severity of poverty.

While Awuah and Addaney (2016) provide another empirical evidence to support the argument that there is positive relationship between microfinance and SMEs growth in Kenya. This study is a survey – based approach and employ data from 152 respondents. After getting financing from microfinance, there is an evident that the level of revenue, profit and assets of the respondents have increased. Furthermore, the results also provide that non – financial services and products of the microfinance institution such as managerial training and business consultation services also significant as major contribution in increasing the growth of SMEs.

Thujo (2015) investigates the effect of microfinance services on growth of SMEs in Nairobi. The variables used in the estimation consist of the amount of microloan, number of training, total savings done by the SMEs in microfinance institutions and legal composition. The results show that microfinance services (the amount of financing, training and savings) have a positive effect on SME growth. The result find an interesting result that the amount of microloan alone has a negative impact. However, this study concludes that there is a strong positive relationship between combined microfinance services and company growth.

In addition, Mohamed and Al-Shaigi (2017) analyze the effect of microfinance on poverty

reduction using the case of Sudan. The study using primary data gathered from interview and questionnaires. They use three dimensions to evaluate the performance of microfinance : outreach, sustainability and business development. The result show that business development is positively influenced by microfinance in the sense that it can increase the level of employment, while microfinance only contribute a moderate effect on outreach to the poor and sustainability.

The study of Siyad (2013) examines how lending from microfinance institution influence the growth of small and medium enterprises in Somalia. The result also corroborates the existing studies that microfinance's lending play as significant factor in affeting the growth of SMEs in Somalia. Moreover, Aldesta (2014) using multiple regression approach finds that microfinance variables proxied by the frequency of financing, duration of business, and the amount of financing have a positive and significant effect on business development.

Antonio (2011) argue that *Baitul Maal wat Tamwil* (BMT) has potential role as a strategic community – based micro lending initiative. The study emphasizes that islamic microfinance play as an alternative source of finance for SMEs in Indonesia.

3 RESEARCH METHOD

The data in this study is used primary data sources, namely original data obtained directly by researchers for purposes related to the problem being studied (malhotra, 2010). Furthermore, the primary data used in this study was obtained from field research (survey – based approach) using a questionnaire. The questionnaire was distributed to respondents who were customers of islamic microfinance institutions in Jakarta, Bogor, Depok, and Tangerang. This study employs a questionnaire distributed through door to door to the location of business / home of the respondent to obtain the data.

Respondents in this study are customers who were getting a sharia microfinance scheme islamic microfinance institutions. The product of islamic microfinance here is also specific which refers to productive financing such as credit financing. This study utilizes customers who had used islamic microfinance services and loan, therefore, the influence of islamic financing could be clearly seen and analyzed.

The questionnaire was adapted from past studies. A total of 160 survey questionnaires were distributed to customers who are taking islamic micro financing scheme from 4 islamic microfinance institution located in Jakarta, Bogor, Depok, and Tangerang.

Institution consists of 2 Baitul Maal wa Tamwil and 2 Bank Pembiayaan Rakyat Syariah (BPRS). The total samples in this research are consist of 160 respondents.

In this study, the method used in sampling is nonprobability sampling, and using convenience sampling technique. Convenience sampling or incidental is a sample determination technique selected by chance, ie anyone who accidentally meets the researcher and can be used as a suitable sample for the data source (Sugiyono, 2017).

The independent variables are financing frequency, average amount of financing, duration of financing, and also training. There are also control variables such as age, education, marital status, gender, business age, and business location. While dependent variable used in this study is profit growth after receiving islamic microfinance to proxy the growth of SMEs. Using multiple regression, this study estimate the following estimation :

$$growth = \alpha_0 + \beta_i SC + \beta_j Business + \beta_k Microfinance + \mu$$

where :

growth : business growth

SC : vector of respondents's socio – demographic factors

Business : vector of respondent's business characteristics

Microfinance : vector of islamic microfinance variables

The detail of the definition of each variables are given in the following table :

Table 1: Variable Definition

Variable	Definition
Growth	profit growth
Socio – demographic variables : Age	Age of the respondents
Education	Education category : 1 = unschooled 2 = primary school = junior high school = high school = diploma = undergraduate
Marital status Gender	1= if married; 0= otherwise 1= man;0=otherwise

Business characteristics : Bizage	Age of business
Bizloc	Location of business 1=commercial/market 0=otherwise
Islamic microfinance : FD	Financing duration
FS	The average amount of financing
FF	Financing frequency
Training	Receive managerial training 1=if yes 0 otherwise

4 RESULT

Descriptive Statistics

This study employ primary data with total number of samples are 160 respondents. The data shows that 100 out of 160 respondents are man, and the rest respondents are woman. Therefore, the proportion of the samples are 62% man and around 38% respondents are women. Accordingly, customers who use islamic microfinance are dominated by men. The reason behind this might occur because man plays a the head of the family and usually they responsible for owning and running the business. While 46% age of the respondents are ranging from 35 – 44 years old.

While the level of education of the respondents are dominated by respondents who graduated from high school. Total 83 respondents are graduated from high school or this number represents 51.88% from total samples. The second highest level of education is junior high school which represent 24.38%.

From the data, it also can be seen that as many as 53 respondents or around 33.13% have monthly income in the range of Rp. 5,000,001-10,000,000, followed by income groups Rp. 1,000,001-5,000,000, totaling 47 people (29.38%). These two range of income are the two highest among other income categories. Meanwhile, most of respondents or 41.25% respondents run their business mostly taken place in market, the next business locations are located in commercial area which represent 31.88% and 26.88% run their business from home as they located in residential area.

Empirical Results

After fulfilling the classic assumptions requirements, the empirical result is presented in the following table

Table 2: Regression Results

	Profit Growth
Age	-0,064 (0,3680)
Education	0.009 (0.0780)
Marital status	0.810* (0.2959)
Gender	-0.1254 (0.1724)
Bizage	-0.0553 (0.1480)
Bizloc	0.1101 (0.1763)
FD	-0.06574 (0.1219)
FS	0.0321 (0.0580)
FF	0.0585* (0.01968)
Training	0.5999* (0.2341)

Number in parentheses : standard error
Indicates 90% of significance level

The regression result show that only three variables are significant in influencing the growth of SMEs. One variable consists of socio – demographic factor namely marital status, while the islamic microfinance variables proxied by financing frequency and training are significant.

Marital status is significant probably because it can be related to the happiness index which in turn affecting the level of productivity. Sunar (2012) that married workers have fewer absenteeism, lower worker turnover. The results of the study are also supported by the study of Hermawan (2012) and which indicate that marital status affects the increase in business income.

The results obtained from the regression result also indicate that the training received by respondents will lead to increased profit growth. This might happen because the training will provide new knowledge to the entrepreneurs that in turn will lead to an increase in respondent's productivity and knowledge to run the business better. Thuo (2015) show that training provides business and financial skills that are very important for making business decisions.

Financing frequency also find to significantly affect the profit growth of the SMEs. Respondents who receive more credit or loan from islamic microfinance tend to experience an increase in profit growth. This results indicate that along with the use of Islamic microfinance programs taken by respondents, it will open opportunities for respective

respondent to increase their business profits. This can be explained since the more often respondent take the financing, the faster the business turnover will be. This result is also supported by research of Perwitasari (2014) who find that there is a positive influence on the frequency of financing with the large development of SMEs turnover.

5 CONCLUSIONS

Overall, the empirical result from this study support the argument that islamic microfinance is significant to affect the growth of SMEs. Specifically, only financing frequency and training as proxy for islamic microfinance variables are significant and positively related with the profit growth of SMEs. In addition, marital status variables also positively related to profit growth.

However, there are still much room of improvement in this study. The number and the scope of the samples used in this study is limited and might not represent a bigger samples. Better approach and methodology may improve the result and can be done for further research.

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