

An Empirical Analysis of Medan Indonesia MSMEs Persistence based on Capital Structure Behavior, Business Strategy, and Business Operational: A Descriptive Study

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Abstract: The purpose of this study is to explore Medan City-Indonesia Micro, Small, and Medium Enterprises (MSMEs) persistence based on their capital structure behavior, business strategy, and business operational. Most literature in SMEs envisage lack of capital is the most severe constraint for SMEs survival and growth. Furthermore, trade-off and packing theory are commonly used to explore SMEs behavior toward how they seek new capitals. This study conducted from 1st of August 2018 until 15th of October 2018 which used primary data through in-depth interview which used questionnaire to capture the characteristics of Medan Indonesia MSMEs capital structure behavior, business strategy, and business operational that describe their persistence. The research population was targeted all MSMEs that operate in 33 districts of Medan, Indonesia and cluster sampling (area sampling) is used as the study sampling method which come out to 21 districts are selected as the sampling area that lead to 530 MSMEs as the research respondents and covers a period of 2017 to 2018. Descriptive analysis is used with SPSS 18 as the study tool of analysis. The result showed that 72.8 percent in 2018 Medan MSMEs did not apply for new capital such as debts and equities. Moreover, data from finance retainment indicates that the proportion of retain in finance was at 62.6 percent which indicate most of Medan MSMEs used their own retain on earning for operating their business. Furthermore, debts retained were at 61.1 percent which was higher than retain on equities at 56.4 percent. Therefore, this empirical evidence of persistence through analysis of descriptive statistics shows that Medan MSMEs capital structure behavior were highly consistent with packing order theory. Moreover, it showed that financial measures, focus on cost, focus on product quality, and focus on innovation are the main characteristics of Medan MSMEs business strategy. Furthermore, it showed that Medan MSMEs operational were mostly characterized by the used of small number of employees that account from using 1-5 employees and operate less than 5 years.

1 INTRODUCTION

One crucial part of SMEs is persistence in doing business because for those who has persistence meant that they have optimism (Adomako, et al., 2016). Studying aspects on SMEs persistence has been attention-grabbing for most of researchers that focusing in SMEs, namely: persistence of product and process innovation on employment growth according to the size of the firms (Triguero, et al., 2013), persistence of SMEs investment in research and development and growth (Mañez, et al., 2015; Deschryvere, 2013; Ahn, et al., 2017), persistence of SMEs performance (Serrasqueiro & Nunes, 2008),

and persistence SMEs on performing Business Excellence (BE) model (Sternad, et al., 2017). However, there are unseen studies that focus on the SMEs persistence based on their capital structure behavior, business strategy, and business operational, especially at the fourth biggest city in Indonesia which is the capital city of North Sumatera, Medan (WIKIPEDIA, 2018). This paper, therefore, introduces a descriptive exploration of Medan MSMEs in doing business which based on capital structure behavior, business strategy, and business operational that operate at Medan, Indonesia.

All business such as SMEs, firm long-term investment is the blood in running or persistence the business game which is called as firm capital structure. Capital structure behavior on SMEs is distinctly difference than those in large company, this is because SMEs financing exhibits considerable contrast when compared to large enterprises which point out finance theory is not established with the small business in mind Ang in (Daskalakis, et al., 2017). Study which have been done by Matias & Serrasqueiro (2017) that examined the behavior of 11.016 Portuguese SMEs and conclude that Portuguese SMEs capital structure differs across regions with the impact of firm size, age, profitability, asset structure, and growth on firm debt. Furthermore, Burgstaller & Wagner (2015) in their study on 470 SMEs that classified as family firm revealed that debt is relatively prefer rather than other external capital injection to the company, whether the family firm controlled by founders or not. Hence, most studies conclude that the capital structure behavior of SMEs are highly consistent with packing order theory (Daskalakis, et al., 2017; Matias & Serrasqueiro, 2017; Burgstaller & Wagner, 2015; Xiang & Worthington, 2015; Xiang, et al., 2015).

Most strategic studies focus on large enterprises such as competitive strategies and strategic groups (Parnell, et al., 2015). Study on Australia SMEs business strategy, Xiang & Worthington (2015) reveals that SMEs that focus on innovations are more likely to obtain debt. Moreover, longitudinal study of internalization strategy on Canadian SMEs Sui & Baum (2014) reported that no single strategy is superior however internalization strategy moderates to Canadian SMEs survival as the relative important of resources. Moreover, in a time of crisis KOSSYVA, et al., (2014) suggest that co-opetition could be an applicable business strategy for SMEs.

There are many studies that focus on supply chain management and information system which are considered as two important application in optimization of firm outcome performance. Comparative study on Turkey and Bulgarian SMEs, Tatoglu, et al., (2015) shows that supply chain management and information system positively influence SMEs operational which Turkey SMEs had higher application on supply chain management rather than Bulgarian. Furthermore, Yadav, et al., (2018) conducted simultaneous equation modelling to analyze lean implementation toward operational performance of 425 Indian SMEs which reveals that operational performance of Indian SMEs are positively related to lean implementation.

This paper used Xiang & Worthington, (2015) key explanatory variables in explaining Medan

MSMEs capital structure behavior, business strategy, and business operational.

2 THEORETICAL FRAMEWORK

Theory and mechanism toward combining debt and equity to financing business activities with a systematically approach is called capital structure theory (Ross, 2018). Moreover, Xiang & Worthington, (2015) find evidence that Australian SMEs financial behavior could be explained by packing order theory and agency cost theory of capital structure theory. Evidence from SMEs at Portugal peripheral region through LSDVC dynamic estimator Serrasqueiro & Caetano, (2015) conclude that the most profitable and oldest SMEs resort less to debt, which verify the forecast of Packing-Order Theory, while SMEs with greater size and resort more to debt verify the forecast of Packing Order Theory and Trade-off Theory.

Modigliani and Miller introduce Trade-off theory or static trade-off theory which states that a company could lower its weighted average cost of capital through capital structure with debt over equity with assumption of debt payments are tax deductible and debt financing is initially cheaper than equity financing (Tarver, 2018). Moreover, a company should favor to finance itself first internally through retained earnings, however, if this source of financing is unavailable then finance itself through debt and if it not enough then as a last resort, a company should finance itself through the issuing of new equity (Tarver, 2018; Zoppa & McMahan, 2002; Zeidan, et al., 2017). Therefore, these two theories are emphasizing which sources of capital that a company favor most.

Applying a specific action through generate a plan to achieve a specific goal is called a strategy (Charles, 2018). There are some specific strategies in understanding product strengths, adjusting price, or acquiring another business of SMEs such as, namely, growth strategy, product differentiation strategy, price-skimming strategy, acquisition strategy (Suttle, 2018). Furthermore, Leonard (2018) presents five types of business strategy in order to satisfy customer needs, explicitly, cost leadership, differentiation, focus low cost, focus differentiation, and integrated low cost/differentiation. In conclusion, a strategy is used by businesses is to ensure sustainability of company growth and generate money could be established.

Business operational is defined as everything that occur within a company to maintain it operation and earning money (Shopify Inc [CA], 2018).

Furthermore, there are four business operation to consider, namely, process, staffing, location, and equipment or technology (Shopify Inc [CA], 2018). Moreover, Lacoma (2018) concludes that there are four keys elements of business operation, explicitly, supply, efficiency, reliability and adaptability, and quality control.

This study refers to the study of Xiang & Worthington (2015) key explanatory variables, which capital structure behavior regarded from applied for additional finance (FINA), applied for additional debt finance (DEBT), applied for additional equity finance (EQUI), availability of finance (AFINA), availability of Debt (ADEBT), availability of equity (AEQUI). Moreover, in seeing business strategy, viewed from focus on financial measures (FOCUF), focus on cost measures (FOCUC), focus on operational measures (FOCUO), focus on quality measures (FOCUQ), focus on innovation (FOCUI), focus on human resources (FOCUH), and acquired written business strategy or written business plan (PLAN). Furthermore, business operational refers to no employee (SIZE01), 1-5 employees used (SIZE02), 6-20 employees used (SIZE03), less than 5 years business operate (AGE01), operate 6 – 20 years business operate (AGE02), operate more than 20 years (AGE03), doing an export of its goods or services (EXP), doing an importing of goods or services (IMP).

In this sense, the study seeks answers to the following questions:

1. What percentage of Medan MSMEs applies additional finance (FINA), debt (DEBT), and equity (EQUI) in 2018?
2. What proportion of Medan MSMEs has the availability of finance (AFINA), debt (ADEBT), equity (AEQUI)?
3. What percentage of Medan MSMEs that focus on financial measures (FOCUF), cost measures (FOCUC), operational measures (FOCUO), quality measures (FOCUQ), innovation (FOCUI), human resources measure (FOCUH), and acquired written business strategy or written business plan (PLAN)?
4. What proportion of Medan MSMEs on their operational measures which refers to no employee (SIZE01), 1-5 employees used (SIZE02), 6-20 employees used (SIZE03), operate less than 5 years (AGE01), operate 6 – 20 years (AGE02), operate more than 20 years (AGE03), doing an export of its goods or services (EXP), doing an importing of goods or services (IMP)?

3 RESEARCH METHOD

This study is descriptive exploration research that used descriptive statistics analysis which conducted through in-depth interviews via questionnaire which based on the study of Xiang & Worthington (2015). Targeted population is 751 Medan MSMEs that has been recorded by the government of Medan City through all in 33 districts in 2018. This research used cluster sampling method which picked 21 districts randomly as the sampling area and about 530 Medan MSMEs has been gathered based on government of Medan City dataset as sampling data through in-depth interviews from 1st of August 2018 until 15th of October 2018. All four research questions are analyzed through descriptive analysis which SPSS 18 as the calculation tool.

Furthermore, this study used three latent variables. Firstly, capital structure behavior with six manifest variables that refers to additional finance (FINA) with nominal type data, applied for additional debt finance (DEBT) with nominal type data, applied for additional equity finance (EQUI) with nominal type data, availability of finance (AFINA) with nominal type data, availability of Debt (ADEBT) with nominal type data, and availability of equity (AEQUI) with nominal type data. The second latent variable is business strategy with seven manifest variables that viewed from focus on financial measures (FOCUF) with nominal type data, focus on cost measures (FOCUC) with nominal type data, focus on operational measures (FOCUO) with nominal type data, focus on quality measures (FOCUQ) with nominal type data, focus on innovation (FOCUI) with nominal type data, focus on human resources (FOCUH) with nominal type data, and acquired written business strategy or written business plan (PLAN) with nominal type data. Finally, the third latent variable is business operational which covers eight manifest variables that refers to no employee (SIZE01) with nominal type data, 1-5 employees used (SIZE02) with nominal type data, 6-20 employees used (SIZE03) with nominal type data, less than 5 years business operate (AGE01) with nominal type data, operate 6 – 20 years business operate (AGE02) with nominal type data, operate more than 20 years (AGE03) with nominal type data, doing an export of its goods or services (EXP) with nominal type data, doing an importing of goods or services (IMP) with nominal type data.

4 ANALYSIS

Data were obtained via descriptive analysis which organized in frequency and percentage. From 530 Medan MSMEs surveyed data, this study finds the proportion of MSMEs at 21 districts in Medan which is mention in Table 1 presents.

Table 1: Medan MSMEs

		Frequency	Percent	Valid Percent
Valid	Micro Enterprises	439	82.8	82.8
	Small Enterprises	89	16.8	16.8
	Medium Enterprises	2	.4	.4
	Total	530	100.0	100.0

Most MSMEs in Medan are Micro Enterprises with the proportion of 82.8 percent from the total sampling. Moreover, the percentage of small enterprises was at 16.8 percent, and only 0.4 percent were medium enterprises.

Table 2: Type of Medan MSMEs Businesses

	Frequency	Percent	Valid Percent
Small Retailer	349	65.8	65.8
Property	28	5.3	5.3
Grocery	78	14.7	14.7
Agriculture	24	4.5	4.5
Recreation and Culture Services	39	7.4	7.4
Communication Services	6	1.1	1.1
Transportation Services	6	1.1	1.1
Total	530	100.0	100.0

Furthermore, Table 2 shows type of Medan MSMEs Businesses with small retailer was the highest portion of all business types at 65.8 percent and around 14.7 percent was Grocery took the second places after small retailer from overall Medan MSMEs. Moreover, recreation and cultural services was the third place after Grocery with the percentage of 7.4 percent. Business in property was the fourth biggest business type at Medan with a proportion of 5.3 percent. Agriculture placed in fifth place with a percentage of 4.5 percent. Finally, communication and transportation services had the same place with the proportion of 1.1 percent.

Table 3: Medan MSMEs Apply/Not Apply for Finance in 2018

Apply for Debt and Equity (FINA)			
	Frequency	Percent	Valid Percent
Not Apply	386	72.8	72.8

Apply	144	27.2	27.2
Total	530	100.0	100.0
Apply for Equity (EQUI)			
	Frequency	Percent	Valid Percent
Not Apply	394	74.3	74.3
Apply	136	25.7	25.7
Total	530	100.0	100.0
Apply for Debt (DEBT)			
	Frequency	Percent	Valid Percent
Not Apply	379	71.5	71.5
Apply	151	28.5	28.5
Total	530	100.0	100.0

Table 3 above showed that most of Medan MSMEs did not apply for debt and equity with the proportion of 72.8 percent and only 27.2 percent applied for debt and equity. Furthermore, the table also showed the percentage of 25.7 percent Medan MSMEs applied for equity and 74.3 percent were not. Moreover, only 28.5 percent Medan MSMEs applied for debt and 71.5 percent were not.

Table 4: Finance Retainment of Medan MSMEs 2018

Retainment of Finance (AFINA)			
	Frequency	Percent	Valid Percent
Not Retain	198	37.4	37.4
Retain	332	62.6	62.6
Total	530	100.0	100.0
Retainment of Debt (ADEBT)			
	Frequency	Percent	Valid Percent
Not Retain	206	38.9	38.9
Retain	324	61.1	61.1
Total	530	100.0	100.0

Table 5: Medan MSMEs Retainment of Equity in 2018

Retainment of Equity (AEQUI)			
	Frequency	Percent	Valid Percent
Not Retain	230	43.4	43.5
Retain	299	56.4	56.5
Total	529	99.8	100.0
Missing	System	1	.2
Total	530	100.0	

Table 4 and 5 shows the retainment of Medan MSMEs in Debts and Equities. Table 4.4 concluded that in 2018, 62.6 percent Medan MSMEs retain on Finance. 61.1 percent showed that Medan MSMEs had retainment in debt and 56.4 percent retainment in equity based on table 5.

Table 6: Medan MSMEs Persistence based on Business Strategy 2018

Focus on Financial Measures (FOCUF)			
	Frequency	Percent	Valid Percent
Not Focus	202	38.1	38.1
Focus	328	61.9	61.9
Total	530	100.0	100.0
Focus on Cost (FOCUC)			
	Frequency	Percent	Valid Percent
Not Focus	212	40.0	40.0
Focus	318	60.0	60.0
Total	530	100.0	100.0
Focus on Operational Process (FOCUO)			
	Frequency	Percent	Valid Percent
Not Focus	273	51.5	51.5
Focus	257	48.5	48.5
Total	530	100.0	100.0
Focus on Product Quality (FOCUQ)			
	Frequency	Percent	Valid Percent
Not Focus	188	35.5	35.5
Focus	342	64.5	64.5
Total	530	100.0	100.0
Focus on Innovation (FOCUI)			
	Frequency	Percent	Valid Percent
Not Focus	232	43.8	43.9
Focus	297	56.0	56.1
Total	529	99.8	100.0
Missing	System	1	.2
Total		530	100.0
Focus on Human Resources (FOCUH)			
	Frequency	Percent	Valid Percent
Not Focus	381	71.9	71.9
Focus	149	28.1	28.1
Total	530	100.0	100.0
Acquired Business Plan (PLAN)			
	Frequency	Percent	Valid Percent

Not Acquired	308	58.1	58.1
Acquired	222	41.9	41.9
Total	530	100.0	100.0

The descriptive measures of Business Strategy at Medan MSMEs show at Table 6. It shows that more than fifty percent Medan MSMEs had business strategy that is based on Innovation, Product quality improvement, cost measures, and finance measures with each proportion of these showed 56 percent, 64 percent, 60 percent, and 61.9 percent respectively. However, acquired business plan, focus on human resources, focus on operational process had been identified less acquired in Medan MSMEs business strategy which each measure showed 41.9 percent, 28.1 percent, 48.5 percent respectively.

Table 7: Medan MSMEs Operational Characteristics 2018

No Utilize Employees (SIZE01)			
	Frequency	Percent	Valid Percent
Utilize Employees	154	29.1	29.1
No Utilize Employees	376	70.9	70.9
Total	530	100.0	100.0
1-5 Employees Used (SIZE02)			
	Frequency	Percent	Valid Percent
No	178	33.6	33.6
Yes	352	66.4	66.4
Total	530	100.0	100.0
6-20 employees used (SIZE03)			
	Frequency	Percent	Valid Percent
No	421	79.4	79.4
Yes	109	20.6	20.6
Total	530	100.0	100.0
Operate Less than 5 years (AGE01)			
	Frequency	Percent	Valid Percent
No	221	41.7	41.7
Yes	309	58.3	58.3
Total	530	100.0	100.0
operate 6 – 20 years (AGE02)			
	Frequency	Percent	Valid Percent

No	421	79.4	79.4
Yes	109	20.6	20.6
Total	530	100.0	100.0
Operate more than 20 years (AGE03)			
	Frequency	Percent	Valid Percent
No	489	92.3	92.3
Yes	41	7.7	7.7
Total	530	100.0	100.0
Doing an export (EXP)			
	Frequency	Percent	Valid Percent
No	508	95.8	95.8
Yes	22	4.2	4.2
Total	530	100.0	100.0
Doing Import (IMP)			
	Frequency	Percent	Valid Percent
No	463	87.4	87.4
Yes	67	12.6	12.6
Total	530	100.0	100.0

Table 7 represents Medan MSMEs operational characteristics in 2018 from utilizing employees until doing import of goods and services. Table 7 revealed that most Medan MSMEs Operational characteristics were no utilizing of employees, using employees in a number from 1 – 5 employees, and operate less than 5 years which each proportion of these showed 70.9 percent, 66.4 percent, and 58.3 percent.

5 RESULTS

Explanation of the research questions one and two are describing the persistence in doing business of Medan MSMEs based on capital structure behavior. The result showed that 72.8 percent in 2018 Medan MSMEs did not apply for new capital such as debts and equities. Moreover, data from finance retainment indicates that the proportion of retain in finance was at 62.6 percent which indicate most of Medan MSMEs used their own retain on earning for operating their business. Furthermore, debts retained were at 61.1 percent which was higher than retain on equities at 56.4 percent. Therefore, this empirical evidence of persistence through analysis of descriptive statistics shows that Medan MSMEs capital structure behavior were highly consistent with packing order theory.

Medan MSMEs persistence on doing business based on Business strategy was showed by answering the third research question. The result showed that financial measures, focus on cost, focus on product quality, and focus on innovation are the main characteristics of Medan MSMEs business strategy.

The last answer of the research question is describing the finding of Medan MSMEs persistence in doing business based on Business Operational Characteristics. It showed that Medan MSMEs operational were mostly characterized by the used of small number of employees that account from using 1-5 employees and operate less than 5 years..

6 CONCLUSIONS

This research reveals fascinating fact that the characteristics of Medan MSMEs persistence in doing business based on capital structure is highly consistent with packing order theory rather than static trade-off theory. Moreover, financial measures, focus on cost, focus on product quality, and focus on innovation are the main characteristic persistence in doing business based on business strategy. Furthermore, the used of small number of employees that account from using 1-5 employees and operate less than 5 years are the most characteristics of persistence in doing business based on business operational characteristics.

This study is descriptive in nature and restricted to the micro, small, and medium (MSMEs) in Medan, Indonesia only. Therefore, future researchers are suggested to obtain more in-depth interviews with longer period in observing MSMEs through panel data which could leads more robust result and could bring more clarity in MSMEs literature and government policies.

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