The Financing Model for Micro-Enterprises During the Covid-19 Pandemic: BMT Level

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ABSTRACT

Most entrepreneurs in Indonesia are in the micro business sector, which has been seriously affected by the Covid 19 pandemic. As a result, they are trapped in high-interest loans. This condition worsened their business when they were unable to pay their obligations. This study analyzes descriptively qualitatively the financing model for micro-enterprises during the Covid-19 pandemic. The descriptive analysis maps the problems of micro-enterprises and ongoing financing schemes and finds a more appropriate model. The research sample was 156 small traders receiving financing from the Baitul Maal wa Tamwil Islamic Microfinance Institution, with a maximum ceiling of Rp.20,000,000.00. The results of the study show that micro-enterprises are dependent on high-interest loans with short terms due to their convenience and family-friendly approach. Other findings show that interest-free Sharia financing schemes, with a speed of service, ease of procedures, and family relationships, are in great demand by micro-entrepreneurs, even though the profit sharing or margins are expensive.

Keywords: Islamic Microfinance, Covid-19 pandemic, Model

INTRODUCTION

The Covid 19 pandemic has negatively impacted micro and small businesses due to the cessation of business activities (Ozili, 2020). Ultimately, micro-entrepreneurs experience severe problems, increasing the poverty rate and exacerbating existing poverty levels (Handfield et al., 2020). Various social activity restrictions give micro-entrepreneurs little income to cover their daily needs

(Nayakkara, 2016). In the end, many of them are trapped in high-interest loans, further burdening their economic conditions.

Microcredit schemes for small businesses are very burdensome (Tan and Lin, 2015) and must follow their business cycle. Meanwhile, social, high-interest loan schemes have created increasingly complex problems (Nayakkara and Stewart, 2014). However, micro-entrepreneurs are generally very practical in their efforts to cover their capital needs.

The choice of seeking microloans in non-formal institutions and even individuals are more influenced by convenience and speed factors (Rogally, 1996). A good service approach and stronger family relationships often make micro-entrepreneurs unable to calculate an enormous economic burden, not even comparable to their business results, so it is very burdensome (Tan and Lin, 2015). Lenders often offer attractive facilities, so micro-entrepreneurs cannot distinguish between the need for funding to increase their business or the desire to get fast funds.

The familial approach model makes micro-entrepreneurs careless in calculating the loan installment burden, principal, interest, and fines. Microfinance, with speed and ease, actually has a high credit risk (Khandker, 1996). Therefore, setting high interest and penalties is also part of an effort to cover this risk (Wang, 2018). From a risk management perspective, income provision is part of a financing risk mitigation technique (Wang, 2020). Therefore, calculating the credit selling price has considered the level of credit risk that will occur.

The problems of micro-enterprises and microfinance should have a strong correlation (Alam, 2010). This means that the microfinance model can answer micro-enterprises needs and the various characteristics of entrepreneurs and their businesses. This condition is an obstacle for Islamic banks in financing microbusinesses. They are often called unbankable even though it is feasible. Micro-entrepreneurs' inability to comply with banking financing procedures and administration is an obstacle in the distribution of micro-finance (Brehanu and Fufa, 2008).

Complex financing procedures with various strict requirements are unsuitable for micro-business conditions (Zheng and Yu, 2013). Banking financing schemes are irrelevant to micro businesses. Bank management should be able to adapt to micro-business requirements, as strong evidence of a commitment to empowering micro-enterprises. But the rules from the Financial Services Authority (OJK), which are very strict in the distribution of financing, become an obstacle in the distribution of microfinance. Therefore, the presence of Islamic Microfinance Institutions that are able to reach micro-entrepreneurs is urgently needed. This research explores micro-enterprises characteristics and financing models relevant to micro-entrepreneurs needs. Islamic Microfinance Institutions, which focus on financing micro-enterprises with members able to reach low-income people, are the objects of research.

LITERATURE REVIEW

Impact of the Micro-Business Pandemic

The COVID-19 pandemic is a health epidemic that severely impacts human life socially, economically, politically, and even religiously (Dayrit and Mendoza, 2020). In the economic realm, the outbreak caused the cessation of various economic activities both on a macro and micro scale (Handfield et al., 2020). According to Ozili (2020), all business sectors are experiencing the same impact due to the covid-19 pandemic.

Research conducted by Nicola et al. (2020) concluded that the Covid 19 pandemic impacted the cessation of the economy in almost all sectors. The impact has been felt in the financial services sector due to decreased customer installments, thus increasing problem financing (Wojcik and Ioannou, 2020). The opposite condition occurs because, at the same time, many fund owners take their funds to cover their necessities of life, so a lot of cash flows out (Akhtaruzzaman et al., 2020).

Micro-enterprises feel a severe impact because the character of their business is daily with limited income. Restrictions on social activities and rising unemployment rates have exacerbated micro-business conditions (Susilawati et al., 2020). The business risks arising from the pandemic are also very high (Heo et al., 2020). This risk is more influenced by the existence of a tightening policy so that many businesses are not running. For financial institutions, high business risk is one of the essential factors that makes it not channel financing and becomes an obstacle to channeling financing (Mahfudz, 2020). Another impact shows increasingly limited micro business capital.

Micro businesses with daily turnover require easy and fast capital turnover. Even though microcredit has a high risk (Zheng and Yu, 2013), micro-business financing directly impacts increasing income (Lin, 2016). Therefore, a more appropriate approach is needed for financial institutions in financing micro-enterprises. Micro businesses need material capital, assistance, fast service, and a more intensive social approach (Rashid and Ejaz, 2019).

Microfinance

According to Bank Indonesia Regulation Number. 14/22/PBI/2012, which was later revised in Bank Indonesia Regulation No. 17/12/PBI/2015, what is meant by Micro Business Credit or what is often referred to as Micro Credit is credit or capital loans given to business actors who fall into the category of Micro Enterprises, Small Enterprises, or Medium Enterprises. Micro Enterprises are productive businesses owned by individuals and/or individual business entities which meet the criteria for micro-enterprises as stipulated in Law Number 20 of 2008 concerning Micro, Small, and Medium Enterprises, namely having a maximum net worth of Rp. 50,000,000 (fifty million rupiahs) excluding land and buildings for business premises; or have annual sales of at most Rp. 300,000,000 (three hundred million rupiahs).

From a Sharia perspective, credit or loan terminology is known as financing. This study uses the term financing because what is being analyzed is financing with the Sharia system. For micro businesses, financing is vital because it can encourage business productivity and meet the company's operational needs (Lin, 2016).

The familial approach to the microfinance model emphasizes the importance of respecting the interests of all parties, as built-in stakeholder theory (Fiordilisi & Molineux, 2010). His research found that the interests of all stakeholders influence bank efficiency, financing risk, and profitability. It is also possible for a stakeholder approach to reduce fraud and increase company productivity (Adegbite & Amaeshi, 2012).

The contribution of all parties in suppressing negative actions that can harm the company is easier to control because all stakeholders feel they own the company. Putting the interests of all parties working together in a balanced manner becomes an excellent social capital. Each party's morals and responsibilities can encourage creativity and enhance cooperation (Mustakalio & Zahro, 2012).

Usman and Tasmin's research (2016) regarding microfinance with a stewardship approach found that one of the strengths of microfinance lies in assisting customers on an ongoing basis. With assistance, microfinance is able to increase customer income, welfare, and even education for their children (Rashid & Ejaz, 2019).

According to El Ebrashi et al. (2018), financing with a profit-sharing system can build better social relations than other contracts between the financier and the recipient. Mutual social relations can increase trust and become excellent social capital (Suhendri & Fera, 2019). With a social approach, microfinance is able to suppress unhealthy financing practices such as conflict of interest, moral hazard, and adverse selection (Mirakhor & Zaidi, 2007).

Besides that, the financing of the profit-sharing model is able to build better morale and business ethics for both parties (Usman & Tasmin, 2016). Even research by Saad et al. (2013) shows that the Islamic financing system has a mutual social relationship. It can reduce financing risks and increase profitability and socio-economic development in the long term. The effectiveness of microfinance at Biatul Maal wat Tamwil is also influenced by a management control model that works well (Sartini, 2014).

The microfinance model with a socio-economic assistance approach has been studied by Arsyanti and Kassim (2017). The results show that customers need financial assistance and education and correlate highly with financing success. The higher the level of financial literacy of the customer, the greater the moral responsibility to return the financing following the agreement (Rashid & Ejaz, 2019). Even during the Covid 19 pandemic, it turned out that customers still had high loyalty to Islamic banks because of good empathy from management (Riduwan et al., 2022).

RESEARCH METHOD

Population and Sample

This research took the population of microfinance recipients from the Baitul Maal wa Tamwil (BMT) Sharia Microfinance Institution in Indonesia. They come from various traditional markets such as Pekalongan, Pasuruan, Rembang, Solo, Semarang, Bantul, Sleman, Kulonprogo, and Gunungkidul. This location was chosen because most micro traders sell daily and receive financing facilities from BMT. The sample was determined by positive sampling with the criteria of a maximum financing amount of IDR 20,000,000.00 (twenty million rupiah), daily installment pattern, daily trading, and willingness to be interviewed. The total sample that was successfully interviewed was 156 small traders, with a ratio of 72% women and 28% men. Apart from that, researchers also conducted interviews with the marketing department and managers or administrators at BMT, namely Bahtera, Bina Umat Sejahtera, Sidogiri, Bina Ihsanul Fikri, Dana Insani, Arofah, An Nikmah, Niten, and Itqon. BMT was chosen because it finances micro entrepreneurs according to the criteria expected by researchers. An additional sample of 14 BMT employees and administrators.

Data and Analysis

The data that will be analyzed is primary and secondary data obtained through direct interviews and filling out questionnaires, both for micro entrepreneurs and BMT employees and officials. Interviews were conducted in groups and individuals taking into account the conditions of micro businesses. The primary data in question includes; business conditions during the pandemic, available financing facilities, experienced financing procedures, installment procedures, financing ceilings, and the amount of margin or profit sharing. Meanwhile, secondary data was obtained through related official BMT publications and the 2020-2022 annual report. Interviews with marketing employees and BMT officials were conducted to strengthen research findings in the field and synchronize primary data with secondary data.

Meanwhile, secondary data was obtained through official BMT publications and the 2020-2022 annual report. Interviews with marketing personnel and BMT officials were conducted to strengthen research findings in the field and synchronize primary data with secondary data. The results of the interviews in the form of primary data and documents obtained from the relevant BMT as secondary data were analyzed using a qualitative descriptive approach. Data on micro business problems and micro financing models at BMT were explored in depth by confirming field findings with theory and secondary data. Various theories regarding microfinance have become analytical tools used to draw conclusions. Conclusions are drawn by classifying various micro business problems to determine the problem map, formulation of financing models that have been implemented, and recommendations from BMT managers.

RESULTS AND DISCUSSION

Microfinance positively affects small entrepreneurs because it can increase their business capacity (Rehman et al., 2015) and reduce poverty (Acha, 2012). Entrepreneurs' interest in microfinance is more due to the ease of procedures and the low valuation of collateral (Alam, 2010). One of the advantages of microfinance is to increase income and the flexibility of financing schemes (Rashid & Ejaz, 2019).

Another factor that influences micro-entrepreneurs interest in taking financing is easy access to financing (Woller, 1999). Finance officers often come to borrowers so they only need a short time to pay their installments. The term pick up the ball effectively increases borrower loyalty because there is more intensive communication. This model can encourage better relationships between financiers and recipients of financing and increase customer capacity (Manaf, 2017).

Fast microeconomic turnover also requires speed in financing services (Acha, 2012). Micro customers often need quick bailouts to cover their business needs. Besides, the relatively short payback period with daily installments is more desirable because of the income or results of selling every day (Al-Shami, 2014). Ease and fast access to financing are vital factors in microfinance services to compete with other financing schemes (Dasgupta & Malay, 2013).

Jack and Roland (2016) stated that gender factors also influence the success of microfinance. Women's groups generally have greater responsibility in managing loans. Research findings by Bahta et al. (2017) also state that female borrowers from farmers in Africa can better maintain lenders' trust. However, the environment also plays an essential role in maintaining the loan's reputation because it can control commitments to fulfill financing agreements (Omorodion, 2007). Meanwhile, according to Asim (2009), women who have loans are able to distribute benefits to their families compared to men.

Another factor that influences the interest of micro traders in accessing financing for BMTs is an interest-free (Syariah) financing scheme, both a buying and selling system and profit sharing (Rashid & Ejas, 2019). Especially during the Covid-19 pandemic, the absence of fines and the convenience of installments, such as paying only margin or profit sharing, became another important factor. The buy-and-sell financing scheme provides certainty of payment in the long term. In contrast, the profit-sharing scheme is believed to be more flexible because it is paid according to the results obtained (Ullah, 2015), even though the buying and selling margin is felt to be more expensive. These findings align with the findings of Parveen (2009) and Mahmud (2015). Meanwhile, according to Usman and Tasmin (2016), Islamic microfinance institutions are the top choice because they can be free from usury, which is forbidden. With a variety of fast service facilities, straightforward procedures, and the Sharia system used, it makes micro-entrepreneurs more comfortable using BMT financing services.

CONCLUSION

In conclusion these findings suggest that micro-enterprises rely on high-interest loans with short terms because of their convenient and family-friendly approach. Other findings show that interest-free sharia financing schemes, with speed of service, ease of procedures and family relationships, are in great demand by micro entrepreneurs, even though the profit sharing or margins are expensive.

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