

# MSME\_P2P LENDING

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# The Role of Peer to Peer Lending in Increasing Funding MSMEs

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## ABSTRACT

This study aims to describe the role of technology in the industrial era 4.0, especially alternative funding in the form of Peer to Peer (P2P) Lending in providing funding solutions for MSMEs by referring to the results of several surveys and research. The presence of P2P Lending is the right answer for MSMEs, some of which do not get financial access from financial institutions, especially banks.

## 1. Introduction

Indonesia is a country with enormous natural potential, a large workforce of young workers, and a broad, dynamic market (OECD, 2015). Another potential possessed by Indonesia is having the fourth largest population in the world (World Population Review, 2019). The largest proportion of Indonesia's population is owned by productive, working-age population, which is around sixty percent, which has great potential to increase Indonesia's economic growth.

But the total population of Indonesia has not been met with an increase in the welfare of its population. The productivity of the Indonesian population per capita is estimated at 32% of the productivity per capita of the population of the United States. Therefore, Indonesia needs to find ways to increase GDP per capita, in order to be able to achieve the welfare achieved by other countries (pwc, 2019).

This projection shows that there are 'missed welfare opportunities' that have not been enjoyed by the working-age population in Indonesia. Some working-age populations do not benefit from higher GDP per capita. Efforts to maximize economic potential and access to funding is a major prerequisite for the population of Indonesia (ibcsd, 2015), especially for the portion of the population that is doing business at MSME<sup>1</sup>. Providing equal access to funding will greatly contribute in creating a multiplier effect on the Indonesian economy. One key element that can drive economic growth effectively is the use of credit to increase production capabilities. Based on the ability to disburse loans per GDP, Indonesia has a very low capability when compared to other countries (PWC, 2019).

Since 2004, the Indonesian government has been persistently promoting MSMEs as a driving force for the growth of lower income communities. As a step towards realizing this objective, the government issued a comprehensive reform economic policy known as the New Economic Policy Package in 2007 and 2008. This package includes policies to improve the investment, financial and infrastructure sectors. One of the priority objectives of the New Economic Policy is to strengthen small businesses.

Moreover, the government also issued UU UKM (UU No.20 / 2008), aimed at all government authorities and Bank Indonesia, which are expected to have an impact on SMEs that

were announced in 2012, concerning the Micro Finance Law contained in UU No.1 / 2013 (ILO, 2019).

Indonesia's experience in the economic area proves that **Micro, Small and Medium Enterprises (MSMEs)** plays an **important and strategic role in Indonesia's economic growth**. MSMEs play a role in contributing to economic growth and employment in Indonesia, as well as in distributing the results of economic growth. MSMEs are also resistant to economic crisis. When the economic crisis occurred in the period 1997 - 1998, SMEs were able to stay afloat. After the economic crisis of 1997-1998 the number of MSMEs did not decrease, instead it continued to increase, and was even able to absorb 85 to 107 million workers until 2012. In 2012, the number of employers in Indonesia was 56,539,560 units. Of these, the Micro, Small and Medium Enterprises (MSMEs) amounted to 56,534,592 units or 99.99% (Bank Indonesia, 2015)

Parallel to the development of digital technology in the Industry 4.0 era, Indonesian MSMEs have the opportunity to obtain alternative funding as well as a media to market their products or services online. Which means, digital technology has played an important role for the development of Indonesia's MSMEs. Technology has become one of the driving factors for business productivity, MSME included (Tambunan, 2011). The use of e-commerce in the marketing of MSME products has been effective. Thus, MSMEs are continuously encouraged to go digital (Setiawan & Raharjo, 2019).

If Indonesia focuses on investments in digital technology, particularly in terms of improving digital infrastructure, increasing penetration, and increasing productivity, then the Indonesian economy will reach **USD 150 billion per year by 2025**. This is a condition that cannot be ignored. If Indonesia adopts a holistic digital strategy, it will empower Indonesian companies to win in the digital era and lift Indonesia's economic growth to the next level. As such, Indonesia must be prepared to benefit greatly from the digital revolution to accelerate economic progress in the public and private sectors (Das, Gryseels, Sudhir, & Tan, 2016).

Digital technology helps Indonesian MSMEs grow faster and be internationally competitive. MSMEs that utilize digital technology are able to innovate, make breakthroughs in doing business, and compete in the international market. One form of digital technology in finance that has succeeded in helping the financial difficulties of SMEs, which in the past was a big problem in China for decades, is P2P Lending. In recent years, P2P Lending as a financial industry innovation has been widely accepted by financial markets throughout the world. P2P Lending is proven to be able to connect investors with those who need funding, so it is considered as a solution to solving MSMEs financial problems. A study that examined the use of P2P Lending as an external financial source found that P2P Lending was a major force to help MSMEs in dealing with financial difficulties. P2P Lending is an internet technology application that has been proven to have a significant ability to connect capital owners with individuals or organizations that need funding, making P2P Lending an effective solution to overcome the difficulties of SME financing (Sun, 2015).

## 2. Theories

### 2.1 MSMEs Characteristic

Indonesia does not have a homogenous MSMEs group, but rather diverse, separated into subcategories. They can be easily identified from distinct characteristics in various aspects, such as ways in doing business, market orientation, social-economic profiles of the owners/producers, nature of workers used, adopted organization and management system, level of mechanization

(nature of production process), sources of raw materials and capital, location, external relationships, and proportion of women's involvement as entrepreneurs (Tambunan, 2011).

## 2.2 Fin Tech – Peer to Peer Lending

Fintech is able to provide services that go beyond conventional banking, in terms of money transfer / remittance, crowdfunding, P2P (Peer-to-Peer) / marketplace loans, and others. One of Fintech's services that provides the highest added value, is mobile-payment / e-Wallets. Other services that Fintech provides includes financial consulting, data analysis especially big data, credit assessment, insurance, and others. Fintech services are more than just banks, it can even replace conventional insurance services.

Fintech's excellence is supported by its ability to combine low cost with technology, so that it can operate with a lower margin. It is also supported by the use of intense technology, including onboarding, social networking, crowd knowledge, and big data used for market analysis and credit scoring. The use of AI with cybersecurity that is needed in the use of private key and touch recognition is equally important to ensure customer's trust. There are several companies who are developing Fintech, namely Telecom Fintech (M-PESA), Fintech Social Media (Fidor) and e-commerce Fintech (Alibaba Group).

There are many ways for Bank Fidor to engage customers, such as through social media and the Internet community, making it possible for customers to rate products and assess bank advisers. This method is appreciated by social-media users, as evidenced by the large number of "likes" that can be generated, while at the same time requiring only a low fee. P2P Lending SMAVA applies a concept centered on openness. It carries out the development by facilitating communities where members can share advice in forums and collaborate on product development. In addition, the bank provides a platform in the app store to provide independent services to third parties (Chuen & Low, 2018).

## 3. Methodology

This study uses critical analysis to analyze MSMEs financing constraints in Indonesia by using the results of previous studies, reports and several Indonesian MSME surveys from 2011 to 2019.

## 4. Analysis

### Characteristic of Indonesia's Fintech Lending

Indonesia has a specific features of Fintech Lending atmosphere, because of the characteristic of its market and regulation. The development of Indonesia's Fintech Lending cannot be easily compared to other countries, as the majority of Indonesian SMEs have limited physical and data.

Most of Fintech Lending clients come from the "Credit Invisible"-MSMEs which previously had no access to credit. There are still huge untapped opportunities, particularly outside Java, because of difficulties in physical outreach and data availability.

There is a tendency of over-leveraged debt behavior, hence requiring an integrated lending database to prevent misconduct. Particularly debt refinancing gives off an impression of the top three loan purposes, indicating the potential for 'over-leveraged' debt behavior. So, an integrated database covering conventional and online lending may be required.

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the industry

The development of credit payment is subsequently followed by the development of NPL. OJK is currently implementing TKB90 to guarantee players unveil their credit execution, which may prevent irresponsible conducts.

As the industry develops, adjusting demand and supply in the platform becomes a critical point. Through cooperation with Financial Institutions and tech companies, players may have a progressively steady source of funds, while likewise expanding the use of their loan portfolio in more instances. Capability to develop cooperation becomes a must-have competitive advantage for players.

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Because of supportive regulation and expanding use cases, we predict that Fintech Lending will have the potential to get accumulative loan disbursements in IDR223 Trillion in 2020. This will support to closing IDR 19.3 trillion of MSME financing gap and expanding the credit access of individuals in 2020 by 12.4% (PwC, 2019).

OJK also informed the disbursement of credit through Fintech in Indonesia reached Rp.8.8 trillion (\$534 million) in the period of 7 months to July 2018, over three times compared to achievement in 2017, amounting to Rp2.56 trillion (\$ 175 million). The loan funds came from 66 local Fintech companies that have obtained operating licenses from OJK to engage in P2P Lending.

The Fintech Association in 2019 stated that there were 235 Fintech companies operating in Indonesia, more than half of the total were established in the last two years. In August 2018, 62 local Fintech companies were applying for permission to the OJK. One of Fintech products that are already available for MSMEs in Indonesia is Investree, which lends funds for a period of 1-3 months and several working-capital loans for one year. The total number of Investree customers are 2,600 micro and SME entrepreneurs. There are also other P2P Lending such as Amarthia, which has provided 130,000 loans since 2010, and Gandeng Tangan, which focuses on rural micro entrepreneurs (ILO, 2019).

Based on this description, it shows that P2P Lending is able to be a solution for MSMEs in financing their business operations. The large number of Peer to Peer Lending options requires MSMEs to choose carefully based on the suitability of the amount of loan with the financing requirements, loan term, and the lowest interest rates. In addition, the use of loans is only for productive purposes, namely for working capital and business development. Misuse of the loan will have an impact on the emergence of bad debt which in turn will result in business bankruptcy.

## 5. Conclusion

Peer to peer (P2P) Lending is an appropriate funding method for Indonesian MSMEs. However, the implementation requires assistance from the government, so that MSMEs can borrow wisely. The loan must be productive and must match the amount needed to support the smooth operation of the business.

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