



Comparative Study of Development and Performance Evaluation Sharia Microfinance Institutions in Indonesia

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Abstract

Purpose - This paper aims to determine the role of Islamic Microfinance Institutions (LKMS) in Indonesia and to make comparisons between theory and practice in the field.

Method - The method used is a descriptive qualitative approach in which data collection is taken from a study of various literature and then compared with previous studies related to the discussion.

Result - Sharia Microfinance Institutions theoretically play a role to help improve the national economy and alleviate community poverty by embracing the lower class and all remote areas. Meanwhile, empirically, Islamic Microfinance Institutions have tried to carry out their operational activities in accordance with the provisions and principles of Sharia, but there are still internal and external constraints.

Implication - This study examines Islamic Microfinance Institutions in Indonesia.

Originality - There are differences between theory and practice in Islamic Microfinance Institutions in Indonesia.

Keywords: LKMS, society, lower class



Introduction

Currently, financial institutions for the community are partners in meeting their daily needs. Financial institutions are a place to make it easier to carry out various financial transactions in the current era of globalization. In addition, financial institutions can also be said to have a very important role in the economy of a country. Along with the times, various financial institutions began to grow and develop. This includes financial institutions with Sharia principles. Although the majority of the population in Indonesia is Muslim, the development of Islamic financial institutions in Indonesia can be said to be late compared to other Muslim majority countries.

Based on variations in the level of financial capacity of the people in Indonesia, an institution is needed that can reach various groups, from the lower, middle to upper class. In general, financial institutions can only reach the middle to upper level, for this it requires financial institutions that not only reach people with an upper economic level, but also those with middle to lower economic levels. Therefore, the government took the initiative to establish a Sharia microfinance institution with the hope of providing financial services to the grassroots community to all remote areas with the aim of carrying out poverty alleviation in Indonesia.

Islamic financial institutions are increasingly developing and become an integral part of the economic system in Indonesia after the economic crisis in 1998. Islamic financial institutions that develop are not only in the form of banks, but also non-bank financial institutions, one of which is developing so rapidly is Baitul Mal Wat. Tamwil, hereinafter abbreviated as BMT. BMT is a sharia microfinance institution based on the economic development of the people (small communities). BMT consists of baitul maal which comes from the word bait which means house and maal which means wealth (Lubis and Wajdi, 2000). In other words, BMT is a sharia financial institution that has the characteristics of institutions that promote social elements (zakat management, infaq, shodaqoh) which is oriented towards the interests of the hereafter and the elements of commerce that focus on developing micro-



processing businesses (Ridwan, 2013). This characteristic is different from other institutions such as foundations and cooperatives. Foundations are legal entities engaged in socio-religious and humanitarian fields. Foundations are basically not profit-seeking bodies. Although foundations may establish business entities, these efforts are aimed at realizing these social, religious and humanitarian functions, not merely commercial functions (Wahyono and Margono, 2001). Meanwhile, a cooperative is a social economic institution that is oriented towards economic empowerment of its members, obtaining profits that are prioritized for the welfare of its members.

Thus the characteristics of BMT are different from other institutions. BMT should be established as a separate legal entity even though in its development not all BMTs are legal entities. Whereas the condition of financial institutions that are not yet legally incorporated has legal consequences in Article 59 paragraph (1) of Law of the Republic of Indonesia Number 21 of 2008 concerning Sharia Banking which states that any business activity in the form of raising funds in the form of deposits or in the form of investments is based on sharia principles, Sharia Bank business activities or Sharia Business Units carried out by individuals without a business license from Bank Indonesia will be subject to imprisonment for a minimum of 5 years and a fine of at least Rp. 10,000,000,000, - (ten billion) and a maximum of Rp. 200,000,000,000, - (two hundred billion)

Islamic Microfinance Institutions have the underlying principles in the scope of their activities, which are guided by the Qur'an and Hadith and carry out transactions with contracts in accordance with Sharia principles. From its inception until now, there have been many Islamic Microfinance Institutions, especially those in the form of BMTs in various regions in Indonesia. The existence of the Islamic Microfinance Institution is expected to be able to improve the welfare of the Indonesian people to develop the economy for individuals and the community around them. from the time the government was initiated the establishment of the Islamic Microfinance Institution until now, it is necessary to monitor its effectiveness and performance to see whether it has actually provided many benefits that benefit many parties.



Methods

The research method used is descriptive qualitative analysis method with case studies based on literature review. Data collection was done by collecting literature from previous research, articles in the mass media, and from related websites.

Results and Discussion

Development of LKMS in Indonesia

In talking about economic problems, the current smooth process is strongly influenced by the existence of financial institutions as institutions that take part in smoothing economic activity (Ahmad, Harahap and Ghozali, 2020). During the reign of President Soekarno, the financial system in Indonesia was very restrained and almost collapsed as a result of the policies that had been implemented. In Indonesia, Micro Finance Institutions (LKM) are regulated in Law Number 13 of 2013 concerning Micro Financial Institutions. 18 Islamic microfinance institutions are one of the pillars in the financial intermediation process (Shiddiqy, 2019). And in 1966 there was an economic crisis that was exacerbated by a political crisis which eventually led to a violent transition and brought General Suharto to power. In the hands of President Soeharto, achieving success in establishing a financial system, especially Microfinance Institutions that can be accessed sustainably by people in rural areas. This financial policy triggered the establishment of the Rural Credit Fund Institution (LDKP) in 1970. This LDKP is a post-colonial rural bank movement which is a generic term for several types of credit and small savings institutions that exist, according to their respective regions and this institution is enforced. as a non-bank financial institution. Islamic microfinance institutions are institutions that introduce as an option for people with low incomes to get financing in order to improve their standard of living and get out of poverty (Gina and Effendi, 2015) triggered the establishment of the Rural Credit Fund Institution (LDKP) in 1970. LDKP is a post-colonial rural bank movement which is a generic term for several types of credit and small savings institutions that exist, according to their respective



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In 1972, the provincial governments of West Java and West Sumatra established several non-bank financial institutions called the Kecamatan Perkreditan Institution (LPK). In addition, the Indonesian government also launched the Community Guidance Credit (BIMAS) program in collaboration with Bank Rakyat Indonesia. BRI divides this program into 2 main networks, namely the BRI Village Unit System and KUD. Over time they also developed the Rural General Credit (KUPPEDES), SIMPEDES, and SIMASKOT programs. In 1988, the Indonesian government launched a decision on banking and financial sector reform called the Pakto 88. And one of the effects of this reform was that one type of MFI was born, namely Bank Perkreditan Rakyat (BPR). Furthermore, Indonesia also develops Islamic microfinance institutions that serve the community in terms of collection and financing,



namely Baitul Mal Wat Tamwil (BMT) (Ahmad, 2015). Within the Islamic Microfinance Institution (LKMS), Islamic cooperatives are not just social financial institutions. However, Islamic cooperatives are also a business institution in order to improve the economy of the people (Kamilah, Indah and Nst, 2019). The growth of LKMS in Indonesia (including BMT) continues to increase rapidly. According to Suharto, the development of BMT in 2010 grew on average in terms of assets in the range of 35% - 40%, financing to deposit ratio (funds channelled) is also still around 100 % (Rusydia and Firmansyah, 2018). In Islamic Microfinance Institutions (LKMS), Islamic cooperatives are not just social financial institutions. However, Islamic cooperatives are also a business institution in order to improve the economy of the people (Kamilah, Indah and Nst, 2019). The growth of LKMS in Indonesia (including BMT) continues to increase rapidly. According to Suharto, the development of BMT in 2010 grew on average in terms of assets in the range of 35% - 40%, financing to deposit ratio (funds channelled) is also still around 100 % (Rusydia and Firmansyah, 2018). In Islamic Microfinance Institutions (LKMS), Islamic cooperatives are not just social financial institutions. However, Islamic cooperatives are also a business institution in order to improve the economy of the people (Kamilah, Indah and Nst, 2019). The growth of LKMS in Indonesia (including BMT) continues to increase rapidly. According to Suharto, the development of BMT in 2010 grew on average in terms of assets in the range of 35% - 40%, financing to deposit ratio (funds channelled) is also still around 100 % (Rusydia and Firmansyah, 2018).

The forerunner to the birth of the KJKS BMT was initiated by the Indonesian Muslim Intellectuals Association (ICMI) which then received a response from the Vice President of the Republic of Indonesia at that time, namely Mr. Habibie representing President Soeharto at the ICMI SILAKNAS in Jakarta December 7, 1995 declaring BMT as a National Movement in order to empower the lower classes of society, at the same time inaugurating the establishment of 1000 BMT throughout Indonesia. On July 1, 1999, it was recorded that 1989 BMTs were operating throughout Indonesia (Fitriana,



2016). The birth of BMT was based on a strong desire to participate in the national economic development process through the empowerment of micro and small enterprises, which number around 92 percent. In Indonesia, the definition of Micro Enterprises is regulated in the Law of the Republic of Indonesia Number 20 of 2008 concerning MSMEs. In Chapter I (General Provisions), Article 1 of the law states that a micro business is a productive business owned by individuals and / or individual business entities that meet the criteria of a micro business as stipulated in the law (Riyadi, Effendi and Nursyamsiyah, 2019). It can be said that the role of micro-businesses is still not optimal because they often encounter many problems, one of which is capital. As for micro businesses according to the Decree of the Minister of Finance No. 40 / KMK.06 / 2003 dated January 29, 2003, namely: "(a) Productive businesses owned by families or individuals, (b) Maximum sales of Rp. 100 million per year, (c) Credit submitted for a maximum of Rp. 50 million (Prayogi and Siregar, 2017). This is the effect of many people who do not know financial institutions because of the complicated procedures. In operation, BMT collects funds from the public called third party funds which are then channelled in the form of productive business financing by combining economic activities and social activities based on Sharia principles (Priyadi and Sutardi, 2018). In Indonesia, the classification of MSMEs is regulated based on Law of the Republic of Indonesia Number 20 of 2008 concerning Micro, Small and Medium Enterprises (Paramita and Zulkarnain, 2018). The presence of microfinance institutions, in this case micro-sharia, is a brilliant opportunity to improve the national economy. Besides, it also has a major influence in the process of developing and empowering MSMEs. Law No. 20 of 2008 which includes MSMEs is Micro, Small and Medium Enterprises, which carry out economic activities individually or collectively (Business Entities), to generate profitability and business development and meet the criteria stated in this Law (Wahiddudin, 2019). Poverty alleviation by empowering MSMEs has been blocked by a pattern that is most fundamental in the banking world, namely bankable (Romadoni and Herianingrum, 2020). And when MFIs expand or deepen the reach of lending



to the poor, it will increase the risk of bad credit which leads to a low level of financial sustainability (RE, Hulwati and Rozalinda, 2019). This is because in its development, the ease of access and requirements offered by Islamic microfinance institutions are more relevant to MSME players because of their more flexible nature. for example, in terms of terms and loan amount, the selection is not as stringent as banking requirements or flexibility in disbursement of financing. This is an indicator that the existence of Islamic microfinance institutions is in accordance with the needs of MSME players, which generally require financing according to the scale and nature of small businesses (Paramita and Zulkarnain, 2018). MSMEs have strong characteristics and the ability to save the wheels of the national economy (Wahiddudin, 2019) 20. The influence of developing MSMEs in Indonesia and seeing the role of government in increasing the growth of MSMEs in Indonesia has positive results, both directly and indirectly (Ahmad Husaeni and Kusmayati Dewi, 2019). The contribution of Islamic banking can be maximized,

The development of microfinance institutions began in the late 1990s, with the aim of, among other things, creating job opportunities and income through the creation and development of micro-businesses, increasing the production capacity of micro-businesses, reducing the attachment of rural communities to harvests that are at risk of failure due to the dry season through classifying activities. small businesses that can generate income (Musyafah, 2019). One of the right principles for empowering micro, small and medium enterprises (UMKM) is through the principle of profit sharing. In general, the principle of profit sharing can be carried out in four contracts, namely mudharabah, musyarakah, muzara'ah, and musaqah (Hermanita, 2013) Musharaka is a collaboration between two or more people, where everyone who works together contributes to capital (be it money. or labor) (Marwini and Salam, 2020) mudharabah contract is a special form of partnership (Mashilal, 2020). Loans are the provision of funds by the MFI to the community which must be returned according to what was agreed upon, while financing is the provision of funds by the MFI to the community which



must be returned according to what was agreed with sharia principles (Fransisca, 2020). The things that differentiate between MFIs and LKMS are 1) MFIs apply the profit sharing principle in their transactions and do not apply any form of transactions that bear interest, 2) The relationship between participation in taking risks and receiving profit sharing from a business agreement is the relationship between MFI and its customers not based on debtor-creditor relationship, 3) LKMS separates the two types of funding so that it can be distinguished between the results obtained from their own funds and the results obtained from the savings they receive on the basis of the profit sharing principle, 4) LKMS provides services on a partnership basis such as in the mudharabah and musyarakah contracts, and on sale and purchase basis (murabahah contract) or on lease basis (ijarah contract) and do not provide loan services with interest in cash, 5) LKMS is a multipurpose financial institution because it acts as a commercial MFI, investment and development MFI and 7) MFI works in under the supervision of the Sharia Supervisory Board (DPS) (Sapudin, Ahmad et al., 2017). Islamic microfinance can play an important role in fighting the poverty dilemma, especially in areas where the majority of the population is Muslim (Suzuki, Pramono and Rufidah, 2016).

LKMS in Theory

Baitul maal wa tamwil (BMT) is an integrated independent business center whose contents are at the core of bay al-maal wa at-tamwil with activities to develop productive businesses and invest in increasing productive businesses and investment in improving the quality of economic activities of small, lower and small entrepreneurs by encourage saving activities and support the financing of economic activities (Jenita, 2017). BMT is intended to absorb the aspirations of Muslims in the midst of anxiety, economic activities with the principle of usury, and to support findings to develop empowerment activities for small and medium enterprises (Purwanto, et al. 2018).



Baitul Maal Wat Tamwil (BMT) can be defined as a microfinance institution that is operated on the principle of sharing and growing micro businesses that require capital. Baitul Maal comes from the word Bait which means house and Maal which means property, while Tamwil comes from the word which means development of wealth. So in Indonesian terms it is called the Integrated Independent Business Center. BMT stands for Baitul Mal wat Tamwil, a type of Islamic microfinance institution in Indonesia. Actually BMT is not a bank, but it is operated like a bank (Kholis, 2012). Baitul Maal wat Tamwil (BMT) is a sharia microfinance institution that can support micro-business capital (Hasan, 2019).

In practice, some BMTs choose to form a cooperative business entity, while others are still pre-cooperative. Sharia Financial Services Cooperative Institution (KJKS) is a form of development of BMT with cooperative legal status. The development of cooperatives that offer financial services with Sharia principles, both labeled BMT and KJKS, has been regulated in the Regulation of the Minister of Cooperatives and Small and Medium Enterprises of the Republic of Indonesia No. 16 / Per / M / Kum / IX / 2015 which contains the implementation of savings and loan business activities. and Sharia financing by cooperatives (Priyadi and Sutardi, 2018). Regulation of the Minister of Cooperatives for Small and Medium Enterprises Nomo 16 of 2015 concerning Implementation of Savings and Loans and Sharia Financing which requires all BMTs for organizing Islamic microfinance businesses to have DPS at their respective head offices (Mujib, 2017). The rapid development of BMTs occurred due to the high public demand for financial intermediation services, but on the other hand access to the more formal world of banking was relatively difficult (Zubair, 2016). The purpose of establishing BMT is for the economic welfare of members and society. This is done by providing working capital to the community to become independent and productive. Whereas the function of establishing BMT is 1) To become an intermediary institution between fund owners and managers for the development of productive businesses, 2) Channeling social funds such as zakat, infaq, alms, waqf, and grants, 3) Developing the potential of the



community in order to increase welfare , 4) Improve the quality of human resources to become Islamic professionals so that they can compete in the global era (Priyadi and Sutardi, 2018). In carrying out its business activities, BMT adheres to the principles of: 1) Honesty, is a person's initial capital in carrying out their business activities, 2) Justice, is an important thing in maintaining the benefit of the people, this is shown by the application of the principle of profit sharing, 3) Partnership, in Islam it is highly recommended to work together in goodness, namely efforts to avoid the element of usury, (Ahmad, 2015) 4) Equality, the owner of funds and managers have the same position, which is reflected in the obligations, risks and benefits that are balanced (Priyadi and Sutardi, 2018). BMT operations are based on sharia principles with contracts of sale and purchase (murabahah), cooperation (mudharabah or musyarakah), lease (ijarah), deposit (wadiyah) and bailout (qard) (Lubis et al., 2020). Hadith Rasullullah SAW. say: "Work for your world as if you will live forever and worship for your afterlife as if you will die tomorrow". This hadith should be the main motivator for Muslim communities to change their destiny and get out of poverty (Hejazziey, 2009)

In their transactions, Islamic Microfinance Institutions use contracts that are made between the owner of the capital and the manager, which are as follows:

1. The Tabarru 'contract is a contract that aims to help in order to do good and does not expect any reward to other parties. This contract is divided into several contracts, a) Qard, which is to provide a loan without providing certain conditions and there are no restrictions on repaying the loan or lending without expecting a return, b) Rahn, which is holding the borrower's property as collateral for the funds he has borrowed, c) Hiwalah is the transfer of rights or obligations carried out by the first party who is no longer able to pay it to a second party who has the ability to pay debts to a third party, d) Wakalah is the power of attorney to the power of attorney to carry out certain tasks on behalf of the power of attorney, e) Wadiyah



custody goods or services to be guarded and can be taken back at any time,

2. The Tijarah contract is a profit-oriented contract, for example a) Murabahah is a sale and purchase transaction where the benefits are known to both parties, b) Salam is a sale and purchase transaction by ordering, but the payment is made first with certain conditions, c) Istishna is a sale and purchase transaction by ordering by requiring certain criteria agreed by both parties, c) Ijarah is the transfer of use rights for a good or service within a certain period of time through lease payments which are not / followed by transfer of ownership, d) Musharaka is a collaboration between two parties in a business with the same contribution which benefits and risks are shared according to the agreement e) Mudharabah is a collaboration between two parties in a business with the contribution of one party as an investor and the other as a manager of the amount of profit and the risk borne according to the agreement (Priyadi and Sutardi, 2018).

LKMS Empirically

1. Research conducted by Lasmiatun with the title Role and Government Policy through LKM / LKMS To Create Distributive Welfare and Justice published in the Dimension Journal, Volume 10, Number 2, November 2017 describes financial institutions as one of the institutions that play a role in national development in economic sector. Institutions calling themselves financial institutions have something in common, namely the aspects that accompany their existence. The aspects referred to are public trust, prudence, and a high level of risk. The hope is that MFIs will appear to take an active role in dynamizing the growth and development of the people's economy (grassroots), especially those carried out by the poor. MFIs can do several things, among others, motivating poor families to save and do business together in groups. MFIs can direct poor families to form groups based on savings capital, then form cooperatives as joint



ventures or become members of them. On the other hand, MFIs with existing networks build awareness of the implementation of the spanning responsibility financial system, so that all dynamics in the group become joint responsibility with the aim of improving the welfare of members or the community.

2. Research conducted by Jenita with the title Role of Sharia Microfinance Institutions in Small and Medium Community Economic Empowerment published in the Journal of Financial and Banking Institutions, Volume 2, Number 2, July-December 2017 describes small and medium enterprises in urgent need of the role of the Syari Micro Financial Institution. 'ah, especially in terms of capital used to expand markets and develop their businesses so that they contribute greatly to the national economy. MSMEs are among the business units that rely heavily on LKMS in the long run for the good of the Indonesian economy, no wonder many people are eyeing LKMS,
3. Research conducted by Reni and A.Alhifni with the title Factors causing people's lack of interest in saving at Islamic Microfinance Institutions published in the Journal of Syarikah, Volume 5, Number 1, June 2019 describes that the variables Price, Product, Location, Service, Facility , and Promotion is thought to have an effect on people's lack of interest in saving at LKMS. However, the results of his research show that the price and product variables have a relationship with the community's lack of interest in saving at LKMS, which is because the price offered by LKMS is still relatively high, thus causing a lack of public interest in saving at LKMS. Meanwhile, the products offered by LKMS are still less diverse so that they do not have superior products which are expected to attract people to save at LKMS.
4. The research conducted by M. Paramita and MIZulkarnain entitled The Role of Islamic Microfinance Institutions in Fulfilling the Capital Needs of Micro, Small and Medium Enterprises, published in the



Syarikah Journal, Volume 4, Number 1, June 2018 explains that all MSMEs use capital from LKMS in the form of financing. productive with various uses, namely working capital, investment and consumption. MSMEs that use capital as working capital in trade are used to buy goods with the aim of increasing the quantity of merchandise in order to be able to serve more consumers, or to increase product variation. MSMEs that use capital for investment mostly procure capital goods to maintain the continuity of production activities. Capital goods that are owned by the results of capital include machines, business premises and other products that are durable in nature. Meanwhile, MSMEs that use productive financing funds for personal consumption activities occur due to a lack of income and low ability to manage funds so that they cannot separate between personal funds and funds for business. From the use of capital above, it can be concluded that MSMEs that use their capital for consumption activities tend not to experience an increase in assets.

5. The research conducted by Muhammad Kamal Zubair entitled Analysis of the Sustainability Factors of Islamic Microfinance Institutions published in the Iqtishadia Journal, Volume 9, Number 2, 2016 explains that there are external and internal factors that have an influence on the sustainability of BMT, namely regulatory aspects, aspects of supervision, aspects of infrastructure, aspects of human resources, and aspects of capital. 1) Regulation is one of the infrastructures that greatly affects the performance of BMT. Based on the regression test that has been conducted in this study, it is known that regulation has an effect on the sustainability of BMT. Regulations are needed to protect small savers in terms of avoiding the inability of BMT to pay customer deposits in the event of a large-scale withdrawal of funds due to decreased customer confidence. 2) Effective surveillance is one tool to detect problems early. Based on the regression test that has been carried out in this study, it is known



that the aspect of supervision is proven to have an effect on the sustainability of BMT. Supervision of BMT institutions requires supervisors with special competences because the aspects being supervised are very specific and detailed. This is very important so that BMTs can comply with applicable sharia regulations, 3) Infrastructure is an important factor for BMT institutions which is proven to affect the sustainability of BMTs. Therefore, for the purposes of institutional development to become a sound and sound financial institution, it is necessary to support the availability of adequate institutional infrastructure. 4) The quality of Human Resources (HR) of BMT managers can be seen from the level of formal education of the managers and the frequency of training related to the duties and experiences of the managers. Based on the regression test that has been carried out in this study, it is known that aspects of human resources are proven to have an effect on the sustainability of BMT. Adequate level of education and knowledge among administrators is also one of the key factors for the success of the Small Business Development Incubation Center (Pinbuk) in developing BMT, 5) BMT capital in this case is the fund from the founder of the financial institution who comes from the BMT owner. as well as BMT capital invested in customers and customer capital invested in BMT. Based on the regression test that has been carried out in this study, it is known that it has an effect on the sustainability of BMT. Capital and funding sources BMTs generally have relatively small capital and it is difficult to raise capital if needed. BMT's ability to raise funds is still very limited, even though the number of financing customers that it has to serve is relatively large. For BMTs that have small total assets, the accumulated need for public funds has not been maximally fulfilled. This makes the value of financing provided by BMT not sufficient for community business capital. This means that the limited availability of funds for most BMTs will complicate business development. Capital and funding sources BMTs



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Conclusion

Sharia Microfinance Institutions theoretically play a role to help improve the national economy and alleviate community poverty by embracing the grassroots all over Indonesia. Meanwhile, empirically, Islamic Microfinance Institutions have tried to carry out their operational activities in accordance with the applicable Islamic provisions and principles, although in practice there are still obstacles that come from internal and external Islamic Micro Financial Institutions.



Islamic Microfinance Institutions have more varied products according to technological developments, educate the public to instill a high sense of trust in LKMS, be more selective in channeling capital financing to people who really need it, and improve various other aspects both internal and external so that it can improve competitiveness against other LKM / LKMS.

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