

Transaction Cost Analysis on The Financing of The Baitul Maal Wat Tamwil

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Abstract: The emergence of Sharia microfinance institutions (S-MFIs) BMT has become a hope for micro, small and medium enterprises (MSMEs) pertaining to the improvement of access to capital loans, business, and welfare of MSME entrepreneurs. This study delves deeper into ex-ante and ex-post transaction costs of the BMT financing scheme at MSMEs from the BMT side and formulates strategies for optimizing BMT financing schemes for MSMEs. Constituting the largest contributor to the overall transaction costs at MSMEs, In a bid to reinforce the financing process, the efficiency of ex-ante transaction costs for drafting and ex-post transaction costs for designing and implementing the BMT's governance is required.

Keywords: Sharia Microfinance Institutions; BMT; MSMEs; Transaction Cost

Abstrak: Munculnya lembaga keuangan mikro (LKM) syariah seperti BMT menjadi harapan bagi usaha mikro, kecil, dan menengah (UMKM) guna meningkatkan akses kredit permodalan, peningkatan usaha, dan berujung pada peningkatan kesejahteraan pelaku UMKM. Penelitian ini bertujuan untuk menganalisis biaya transaksi ex-ante dan ex-post pada skema pembiayaan BMT pada UMKM dari sisi BMT; menganalisis biaya transaksi ex-ante dan ex-post pada skema pembiayaan BMT pada UMKM dari sisi UMKM; merumuskan strategi optimalisasi skema pembiayaan BMT terhadap UMKM. Diperlukan efisiensi biaya transaksi ex-ante untuk biaya membuat draft dan biaya transaksi ex-post untuk biaya merancang dan menjalankan tata kelola BMT, karena dua jenis biaya transaksi ini merupakan penyumbang terbesar dari keseluruhan biaya transaksi di UMKM.

Kata Kunci: Lembaga Keuangan Mikro Syariah, BMT, UMKM, Biaya Transaksi

Introduction

Microfinance Institutions (MFIs) give hope to overcome the lack of capital problems for micro, small and medium enterprises (MSMEs) in Indonesia. Based on the Law of the Republic of Indonesia Number 1 of 2013, microfinance institutions are financial institutions specifically established to provide business development services and community empowerment, either through loans or micro-scale business financing to community members, managing deposits, as well as providing business development consulting services that are not solely for profit.

Microfinance institutions are not simply profit-driven, but also have a social mission that includes community development, without compromising its role as a financial intermediary institution (Baskara, 2013). The role of microfinance institutions as intermediaries in financing MSMEs or business loans is expected to overcome the lack of capital for MSMEs. The existence of sharia microfinance institutions is indispensable for the development of a sharia-based economy, especially in empowering small and medium-sized enterprises as well as being the core of populist-based economic strength and the main support for the national economic system (Rusydiaana & Devi, 2018). One of the sharia micro-institutions in Indonesia is Baitul Mal Wat Tamwil (BMT). The profit-loss sharing (*murabaha*) scheme in Islamic finance is one of the MSME financing schemes that Islamic financial institutions frequently offer in Indonesia (Ferawati, Juanda, Syaikat, & Bratakusumah, 2015).

However, the development of BMT in Indonesia is deemed more delayed compared to conventional MFIs. The high transaction cost is one of the reasons for this. Rahman and Dean (2013) stated that high administrative costs are one of the reasons why Islamic microfinance institutions are ineffective. The high administrative cost indicates a problem in Islamic MFIs. Moreover, informal Islamic microfinance institutions in the form of

cooperatives tend to pay more for their membership (Obaidullah & Khan 2008).

Shankar (2006) argues that the high transaction costs at MFIs may be the cause of the inefficiency of BMT in financing MSMEs. The high transaction costs in an interest-free financing system with a profit-loss sharing or *murabaha* scheme are seen to be one of the reasons why MSME actors are hesitant to employ BMT financing. This underlies the need to establish an innovative sharia financing model for MSMEs with lower transaction costs.

The research objectives are to identify and analyze transaction costs in the Baitul Maal Wat Tamwil of sharia MFI financing scheme for MSMEs and to formulate an institutional design based on a transaction cost approach for MSMEs. The relevance of efforts to promote and strengthen MSMEs is linked to the urgency and priority of research since MSMEs contribute positively to the Indonesian economy. This study provides a detailed analysis of the transaction cost of MFIS and MSMEs. This leads to a more in-depth analysis, which sets it apart from previous studies.

The contribution of MSMEs does not correspond to the issues that MSME players experience, particularly in terms of funding. One of the issues that MSME players complain about is high bank fees and interest rates. Although the government has issued the People's Business Credit program (KUR), in practice there are still banks that make it difficult to disburse KUR funds. Besides, the KUR interest rate is still considered burdensome for MSME players. Islamic microfinance institutions are envisioned as a solution for all MSME players, not only Muslims.

Literature review

Research on MFIs is very important because of their role in helping the MSMEs grow. MFIs have the capacity to address the credit needs of impoverished people, particularly in rural regions, and help them improve their standard of living (Notolegowo & Darwanto 2017; Yadav 2014). MFIs

can help MSMEs grow by contributing to their growth and assisting them in the development of their businesses (Ngugi & Kerongo, 2014). A case study of Indian MSMEs reveals that MSMEs can be sustainable and survive not just by managing micro funds obtained from MFIs, but also by having access to MFIs for micro-credit (Ravi & Roy 2014).

In particular, this study aims to improve the performance of Islamic MFIs, especially in terms of MSME financing. The necessity for study on Islamic MFI transaction costs in funding MSMEs stems from the potential of Islamic MFIs, according to Rahman and Dean (2013), who claim that excessive transaction costs are a concern for both conventional and Islamic MFIs. Rahman and Dean (2013) and Ahmed (2002) state something opposite. Ahmed (2002) asserts that one of the potentials of Islamic MFIs is being able to mitigate asymmetric information compared to conventional MFIs. However, Ahmed (2002) is indirectly refuted by Rahman and Dean (2013) who states that high transaction costs are still one of the biggest challenges, which is an indication that Islamic MFIs cannot mitigate asymmetric information. Transaction costs are still an ingrained problem for microfinance institutions, especially in compensation for field labor costs and clients/groups handled (Shankar, 2006).

In order to formulate the transaction costs of MSME financing by BMT, conditions are needed from the institutions themselves. BMT is a microfinance institution that operates according to sharia principles that functions as an economic driver in Islamic boarding schools. The BMT was developed on the initiative and initial capital of local community leaders based on the *Salaam* economic system of security (justice as the core), peace, and prosperity (Kurniasari, Sawarjuono, & Ryandono, 2019). The importance of analyzing transaction costs in BMT is based on the research of Abiad, Cuevas, and Graham (1988), which states that high transaction costs have a regressive effect for members and on the institution itself. Sakti (2013) revealed that institutionally, BMT operations require special improvements in industrial

governance aspects and BMT internal aspects such as operations and management. Rahman and Dean (2013) state that of the three challenges described, high administrative costs are one of the problems in Islamic MFIs in financing MSMEs. Shabrawy (2011) revealed that the implementation of the Grameen Bank system needs to be carried out by Islamic MFIs to improve the performance of Islamic MFIs in financing MSMEs. Regarding the group lending model, the group loan scheme has a positive impact on the development of entrepreneurship and increased welfare (Attanasio et al., 2011).

Pertaining the transaction costs, Kar (2010) revealed that the group loan scheme can assist MSME entrepreneurs in reducing transaction costs, especially for travel costs to the bank, and reducing wage losses. Other studies (Fachini, Ramirez, & De Souza Lima (2008); Swamy & Tulasimala, 2011) prove that group loan schemes better mitigate transaction costs compared to individual schemes. Furthermore, Swamy and Tulasimala (2011) stated that the transaction costs are low in the group loan scheme since it has a faster process.

The amount of transaction costs reflects the institutional design (Listiyanto & Manzilati 2007). The greater the transaction costs show an inefficient institutional design. On the other hand, low transaction costs indicate an efficient institutional design.

Transaction costs can be divided into ex-ante and ex-post transaction fees. Ex-ante costs consist of the costs of drafting, negotiating, and securing the agreement. Meanwhile, ex-post costs include 1) maladaptation costs when the transaction deviates from the required commitments; 2) negotiation/haggling costs incurred when making bilateral efforts to correct eviations after the contract; 3) costs for designing and carrying out activities related to the governance structure in the event of a dispute; 4) binding costs so that the agreement that has been made can be guaranteed (Listiyanto & Manzilati 2007; Williamson 1985; Yustika 2006).

This research is a development of previous studies. Darwanto (2011) explains the strategic role of SMEs in the national economy. Darwanto, Hendarto, and Atmanti (2010) state that SMEs with their locality have higher employment absorption than large industries. Darwanto (2014) further argued that greater development of human resources, particularly related to social capital, is required to improve the performance of Sharia MFIs from an institutional perspective.

Methods

This study was conducted with Islamic microfinance institutions in Central Java as the object of research. The Islamic microfinance institution in this study is Baitul Maal Wat Tamwil (BMT) located in Central Java. The samples of BMT are coded BMT A, BMT B, BMT C, and BMT D. 45 BMT members were also involved as research objects. The sample of this study is depicted in Table 1.

Table 1. Sources of Respondents

Name	Location	Establish	No. of Respondent
BMT A	Semarang	1999	15
BMT B	Semarang	2009	8
BMT C	Demak	1998	9
BMT D	Jepara	1997	13

The sampling technique used was purposive sampling. The BMT members were selected based on the following criteria: 1) members who run MSMEs, can be any field; 2) members taken financing at BMT in the last 2 years; and 3) members domiciled in Central Java. The selected respondents required consent from the BMT and the members considering personal

questions asked. From these techniques, 4 BMTs and 45 BMT members were selected as samples in this study

The increasing growth of BMT in Central Java is the driving force behind this study's choice of BMT as the research object. The data used in this study are primary data and secondary data. Primary data were obtained from interviews with key respondents from the BMT and MSME members or those with financing from BMT. Secondary data was obtained from BMT's financial statements. The data analysis techniques used were data description and comparison.

Result and discussion

This study conducted a study in 4 BMTs located in Central Java, namely BMT A, BMT B, BMT C, and BMT D. BMT A was established in 1999 with IDR 32,000,000,000, and IDR 3,200,000,000 of total assets and net worth respectively. BMT B was established in 2009 with the total assets reaching IDR 4,200,000,000, and a net worth of IDR 16,500,000 per month. BMT C was established in 1998 with total assets of IDR 31,000,000,000, and a net worth of IDR 150,000,000 per month. BMT D was established in 1997 and for some reason, BMT D did not provide a more detailed explanation of the number of assets and also the income earned per month.

Transaction Cost Analysis before the Contract (Ex-Ante)

Drafting Cost

When BMT and MSME members agree to financing transactions, there are a number of activities that incur costs, such as drafting an agreement. The costs incurred when this contract occurs are charged to MSME members in the form of financing discounts. From the results of interviews with the chairman of BMT A, the manager of BMT B, and the head of marketing of BMT C, the discount is 2% of the loan submitted. If the loan is X rupiah, then the loan obtained by the member is: $\{\text{loan} = X - (2\% \times X)\}$. Meanwhile, based on the

results of interviews with the manager of BMT D, the determination of the drafting cost at BMT D is determined based on the proposed financing range. The greater the financing proposed by the member, the greater the transaction fees charged. If it is notated in an equation, then the transaction costs from the drafting cost of BMT A, BMT B, and BMT C are:

$$\text{Transaction fee} = 2\% \times \text{average member loan}$$

Table 2 shows the transaction costs from the drafting costs. The drafting cost is borne to the member (MSMEs), hence no money is spent by the BMT.

Table 2. Drafting Cost (IDR)

No.	BMT	% Drafting Cost	Average Financing (IDR)	Transaction Cost (IDR)	Financing Given (IDR)
1.	A	2%	10,000,000	200,000	9,800,000
2.	B	2%	7,500,000	150,000	7,350,000
3.	C	2%	6,500,000	130,000	6,370,000
4.	D	500,000 (if the loans range from 1,000,000 to 10,000,000)	2,000,000	500,000	1,500,000
Average				245,000	

The determination of the transaction fee of 2% is a standard rule in the BMT SOP, especially at BMT A, B, and C. The determination of 2% is also the result of an agreement from all BMT members. A transaction fee of 2% of the loan is used for administrative purposes, stamp duty, etc. The chairman of BMT A explained that the larger the loan submitted, the higher the transaction costs incurred.

Negotiation Cost

Negotiation costs are costs incurred in negotiating activities between the parties concerned. The cost paid to notaries and lawyers is included in the

negotiation costs. BMT A does not use the services of a notary and lawyer. Meanwhile, BMT B spent IDR 2,200,000 for notaries, BMT C spent IDR 1,650,000 for notaries, while BMT D spent IDR 1,550,000 for notaries. The BMT pays for the negotiation fees, leaving the MSME with no costs incurred.

Table 3. Negotiation Cost on BMT

No.	BMT	Negotiation Fee Details	Negotiation Cost (IDR)
1.	A	There is no negotiation cost	0
2.	B	Notary fee	2,200,000
3.	C	Notary fee	1,650,000
4.	D	Notary fee	1,550,000
Average			1,350,000

Cost for Securing the Agreement

To bind commitments in financing transactions with members, BMT charges fees on members. Because the BMT sample used is a cooperative legal entity, in its business the BMT implements cooperative principles, in which BMT determines principal savings to members as a form of commitment. The cost of this basic deposit is the cost of securing the deal. The amount of principal savings are IDR 100,000 in BMT A, IDR 50,000 in BMT B, IDR 50,000 in BMT C, and the charge for Community Development for Independence of IDR 10,000. The member (MSMEs) bears the cost of securing the agreement; BMT does not bear any cost.

Table 4. Costs of Securing MSME Agreements

No.	Description	Costs of Securing Agreements (IDR)
1.	Average principal savings of 45 members in 4 BMT	73,333

Transaction Cost Analysis after Contract (Ex-Post)

Cost of Adaptation Failure

The post-contract transaction costs include the costs of failure to adapt when the transaction deviates from the agreement. An example of a transaction that deviates from the agreement is when the MSME runs a business that is different from the initial financing agreement. If this occurs, BMT will make some efforts to adhere to the commitment that has been agreed upon by the member. The cost required by BMT is referred to as the cost of adaptation failure. There are differences in the treatment of the BMT in responding to this situation. BMT A, BMT B, BMT C, and BMT D will only reprimand the member, and remind the importance of honesty and commitment that has been agreed upon at the beginning. The BMT also warns that breaching the contract is the same as committing a sin. BMT does not charge any fees as long as the contract has not expired. After the contract expires, BMT will reschedule the agreement. The transaction cost from rescheduling activity is the same as the transaction fee at the time of the contract, which is 2%. Cost of Adaptation failure (if any) will be borne by the member (MSME).

Negotiation Costs in Case of Deviation After Contract

If there is a bad debt recovery from the member, BMT will charge the member. BMT A will apply a *takwid* system by charging fees based on the costs incurred by BMT during a delay in returning from the member in the form of operational costs. The amount of *takwid* is determined by the type of transaction and the length of delay in returning. BMT A is to charge the member a fee of 2% of the monthly installments if the member is in arrears with their financing repayments. It is known that the average monthly installment of BMT A members is IDR 3,312,864. Thus, the estimated amount of negotiation costs, if there is a deviation after the contract at BMT B, is IDR 66,257.28 (2% x 3,312,864). Meanwhile, at BMT C and D, the member will only

be reminded once a month, and if the member does not also have good intentions to complete the funding, BMT will withdraw the guarantee that was agreed upon. Negotiation costs are borne by the member (MSME).

Table 5. Negotiation Costs in Case of MSME Deviations

No.	Description	Negotiation Cost in Case of Deviations (IDR)
1.	The average of <i>takwid</i> cost from 45 members (MSMEs) in 4 BMT	31,579

Governance Cost

The costs of designing and implementing governance are the costs incurred to fulfill obligations to the government. Tax costs, as well as public charges for auditing BMT finances, are included in the costs of designing and implementing effective governance. Of the 4 BMTs, there is a governance fee at BMT B of IDR 295,000.

Table 6. Cost of Governance Implementation in BMT

No.	BMT	Cost of Governance (IDR)
1.	A	0
2.	B	295,000
3.	C	0
4.	D	0
Average		98,333

Meanwhile, from the MSME, the costs of designing and implementing good governance are delineated in Table 7.

Table 7. Cost of Governance in MSME

No.	Description	Cost of Governance (Rp)
1.	Average taxes and fees 45 members in 4 BMT	80,263

Cost of Commitment Binding

The cost of commitment binding is the cost required to maintain the commitment to membership in the BMT. A mandatory deposit is included in this cost. The mandatory deposit at BMT A, B and C is 10,000 while at BMT D is 5,000. It is charged to members (MSMEs), hence no money is paid by the BMT.

Table 8. Cost of Commitment Binding in MSME

No.	Description	Cost of Commitment Binding (IDR)
1.	Average mandatory deposit of 45 members in 4 BMT	10,000

Transaction Cost Analysis in BMT

The discussion section interprets the data obtained in the results section. Table 9 explains the details of ex-ante and ex-post transaction fees from the BMT.

Table 9. Ex-ante and Ex-post Transaction Cost in BMT

Transaction Cost	Description	Average (IDR)
Ex-ante (E.A.)	E.A.1. Drafting Cost	0
	E.A.2. Negotiation Cost	1.350,000
	E.A.3. Securing The Deal Cost	0
Total ex-ante		1,350,000
Ex-post (E.P.)	E.P.1. Adaptation Failure Cost	0
	E.P.2. Negotiation costs in case of deviation after contract	0
	E.P.3. Governance Cost	98,333
	E.P.4. Commitment Binding Cost	0
Total ex-post		98,333
Total ex-ante + ex-post		1,448,333

The average value of ex-post and ex-ante transaction costs was calculated based on data tabulation. The total average ex-ante transaction cost is IDR 1,350,000, and the total average ex-post transaction cost is 98,333. This shows that the transaction costs incurred by BMT for activities before the contract is greater than the transaction costs incurred after the contract. Meanwhile, the total average transaction fee issued by BMT is IDR 1,448,333.

The relationship between transaction costs and BMT financing is shown in Table 10.

Table 10. Percentage of Transaction Costs on BMT Financing

Description	Nominal
Total average BMT Transaction Cost	1,448,333
Total average BMT Financing	15,053,571
Percentage of transaction cost on financing	9.62%

Based on Table 10, the percentage of transaction costs to financing is 9.62%. This shows the high transaction costs incurred by BMT for financing schemes.

Transaction Cost Analysis in MSME

Table 11 explains the details of ex-ante and ex-post transaction fees for MSME as members.

Table 11. Ex-ante and Ex-post Transaction Cost in MSME

Transaction Cost	Description	Average (IDR)
Ex-ante (E.A.)	E.A.1. Drafting Cost	203,684
	E.A.2. Negotiation Cost	0
	E.A.3. Securing The Deal Cost	73,333
Total ex-ante		277,018
Ex-post (E.P.)	E.P.1. Adaptation Failure Cost	0

E.P.2. Negotiation costs in case of deviation after contract	31,579
E.P.3. Governance Cost	80,263
E.P.4. Commitment Binding Cost	10,000
Total ex-post	121,842
Total ex-ante + ex-post	398,860

The average value of ex-post and ex-ante transaction costs was obtained from the data tabulation. The total average ex-ante transaction cost is 277,018, and the total average ex-post transaction cost is IDR 121,842. This shows that the transaction costs incurred by MSMEs for activities before the contract is greater than the transaction costs incurred after the contract. Meanwhile, the total average transaction costs incurred by MSMEs was IDR 398,860.

Table 12. Percentage of Transaction Costs on MSME Financing

Description	Nominal
Total average BMT Transaction Cost	Rp398,860
Total average BMT Financing	Rp15,053,571
Percentage of transaction cost on financing	2.65%

Based on Table 12, the percentage of transaction costs to financing is 2.65%. This demonstrates that the transaction costs incurred by MSMEs for financing schemes are relatively low.

Conclusion

Based on close scrutiny, it can be summed up that transaction costs are quite high among the BMT financing scheme in Central Java as indicated by the percentage of transaction cost reaching 9.62% of the financing granted to members. Meanwhile, from MSME, transaction costs reached 2.65% of the financing. As observed from BMT, it is essential to conduct efficiency for transaction costs prior to the contract on negotiation costs, and after the

contract on designing and implementing costs. Meanwhile, from MSME, it requires to embark efficiency of transaction costs before the contract on the drafting cost and after the contract on the cost of designing and implementing BMT's governance.

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