

A Study on the Impact of Globalization on MSMEs in Indonesia

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Abstract

The purpose of this study is to analyze the impact of globalization on MSMEs in Indonesia in the context of prior of the Covid-19 pandemic. The study applied descriptive qualitative approach and used documentation as the data collection in which the data were retrieved from journals, web, and other relevant sources. The results concluded that MSMEs in Indonesia with 10% contribution had not been able to significantly support the Indonesian economy due to various obstacles. The government has taken various ways to overcome this problem and expected that by 2024 MSMEs can support 17% of the national economy.

Keywords: globalization, economic globalization, MSMEs

INTRODUCTION

Globalization is a term that was getting known in 1980s and had been becoming a popular topic in 1990s. According to the International Monetary Fund (IMF), globalization has four aspects of trade, i.e. transactions, investment, movement of capital or people, and the independence of science. It occurs due to the influence of business processes, economy, natural resources, and socio-culture. It however gives rise to environmental problems such as climate changes, oceanic over-fishing, air pollution, water pollution, and trans-boundary air pollution (Fund, 2000).

Giddens (1991) mentioned that globalization can connect remote places and brings influences on anything regardless the distance and boundaries. Larsson (2001) emphasized this by stating that globalization is a process causing distance and interaction between different parts of the world are getting closer. In the context of economic globalization, intensification and expansion of economic connections around the world become massive. Economic globalization relates to internationalization of trade and finance, increasing power of transnational corporations and large investment by banks, and increasing role of international economic institutions such as the IMF, World Bank, and World Trade Organization (WTO) which are the most often referred to in the context of economic globalization. These three institutions enjoy a special position in making and enforcing global economic rules that promote a significant difference in power between the global North and South (Rohendi, 2014).

Massive flows of capital mediated by digital technologies have boosted trade of goods and services. Migration to cyberspace and creation of new links between national and regional economies have been the way for expanding the reach of the world. Large transnational corporations, strong international economic institutions, and giant regional trade systems such as the Asia Pacific Economic Cooperation (APEC) or the European Union (EU) have emerged as the main building blocks of the 21st century global economic order (Nugroho, 2020).

Economic globalization brings evidence that some national economies have increased their productivity as a result of free trade. It enables millions of people in developing countries such as China and India to be lifted out of poverty. The 2012 World Bank report shows that for the first time the proportion of people living in extreme poverty and earning less than \$1.25 per day was lowered in every developing country in 2005-2008. The progress has been so drastic that the United Nations Millennium Goal for halving extreme poverty had been

successfully achieved it three years ahead of the 2015 deadline. Even though it is apparent that the society gains benefits from specialization, competition, and the spread of technology, it however is less clear about what gains resulted from the trade freedom distributed fairly within and between the population (Kharisma, 2014).

Globalization that creates seemingly borderless country around the world provides formidable challenges for the third world countries. It presents not only opportunities but at the same time challenges and threats. In the early 1990s, Thailand, Indonesia, Malaysia, South Korea, and the Philippines gradually lessened their control over the domestic capital movement to leverage foreign direct investment (Mon et al., 2023). Globalization becomes an opportunity for those who win the competition and a threat for those who lose the competition. The superpowers that own substantial capital and large companies are possibly the threats since they tend to put pressures on respectively developing countries and small companies. Such condition is however unavoidable since the advanced technological developments enabling information available widely has made society becomes an open system (Yuniarto, 2014).

Globalization is most likely driven and controlled by the developed countries that own corporations with monopoly power and oligopoly markets. Corporations need to sustain their businesses (Susanty, 2018) since they can possibly be challenged by MSMEs that have been growing significantly in number in developed and developing countries (Astuti & Gunawan, 2022) by creating network.

The WTO supports development of MSMEs by holding several meetings for discussing ways for strengthening them. The meeting held by the OECD in Italy resulted in a decision to carry out economic restructuring for MSMEs (Hashim, 2015). Similarly, the United Nations Conference on Trade and Development held in Thailand in 2000 resulted in

the decision that instability in the international financial system required immediate attention. European MSMEs that have been focusing on exporting goods to many other countries and neglect the domestic needs has resulted in dependency on foreign suppliers. This is contradictory with the US that has paid attention to the domestic needs while it is exporting.

Ability of MSMEs to exporting and importing and to establish partnerships with large corporations are two strengths of MSMEs. Nevertheless, the development of exports by MSMEs in Indonesia is still behind those by other Asian countries. Figure 1 shows that in 2018 Indonesia's exports were ranked the 5th under that of Singapore, Thailand, Malaysia, and Vietnam. On the other hand, the number of MSMEs in Indonesia has been increasing gradually by 2% on average during 1997-2017 (figure 2). This indicates high potential contribution to the national economy in general and exporting in particularly.

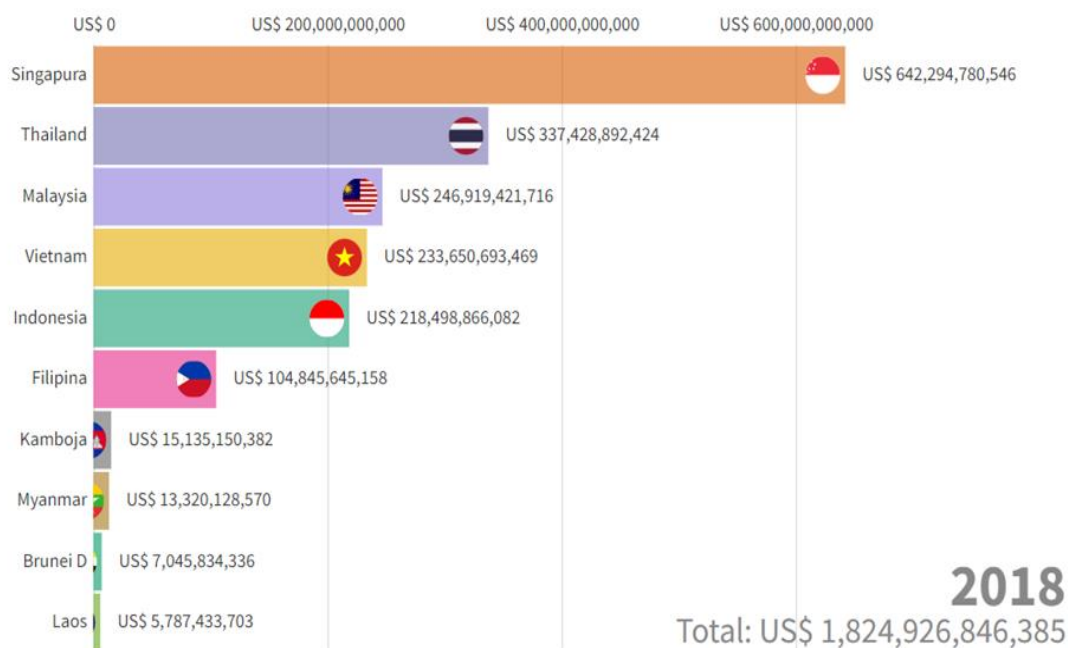


Figure. 1. The Export of Asian Countries

The interesting phenomenon of MSMEs in Indonesia calls for deeper study. This research addresses the development of Indonesian MSMEs in the midst of economic globalization and analyzes if the government efforts for encouraging MSMEs are effective.

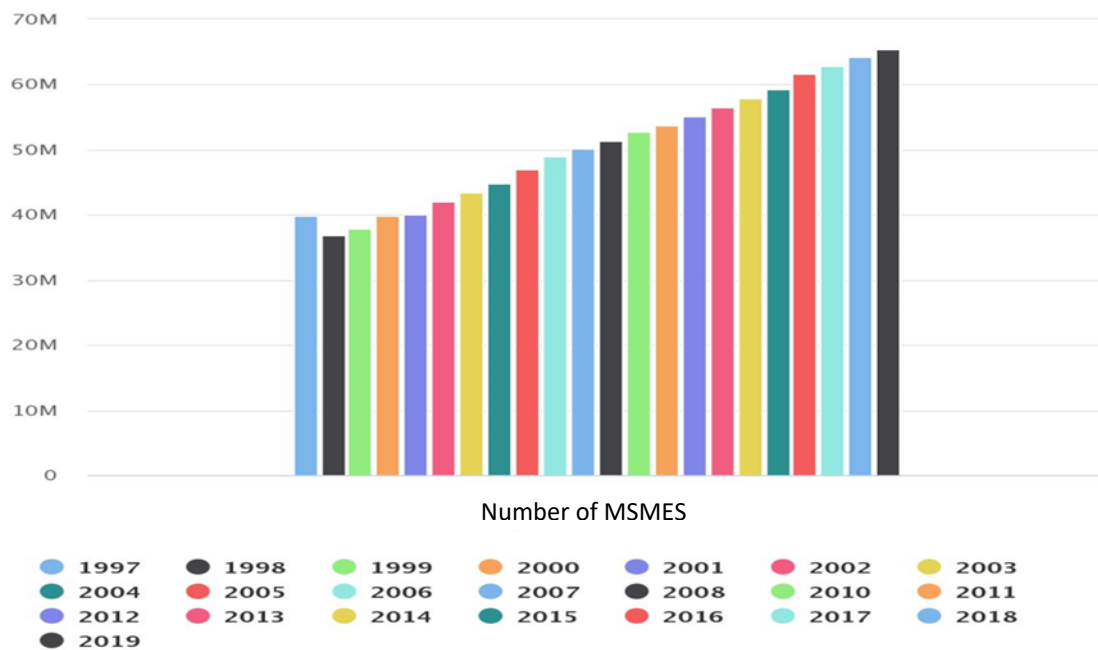


Figure 2. The Number of MSMEs in Indonesia 1997-2019

METHOD

The study applied a quantitative method and used secondary data which were available in the form of graphs, tables, diagrams. The data were gathered from several sources such as research reports, journal articles, government regulations, and textbooks. The study was a library research which include the process of preparing the required equipment, conducting bibliographic study, organizing time, and recording the data (Jaya, 2020). Content and discrete analyses were to analyze the data and critical analysis was applied to a certain level of depth in order to strengthen the ideas.

ADVANTAGES OF A NATION

The theory of absolute advantage developed by Adam Smith refers to advantages of a country over the others'. According to this theory, a nation will be superior over the others if it has absolute advantage. This means that a nation is able to produce goods at lower costs and exchange it for other goods produced more efficiently by others. Importing is thus considerably more beneficial as it will be more expensive to produce the goods themselves and the nation will earn only a small profit. A nation is also absolutely superior to others if it is able to produce goods cannot be made by other nations. (Sahriar, 2019). Since each nation has unique resources and thus has different absolute advantage, each can thus specialize in the production of goods in which it has the absolute advantage and export it in exchange for other goods.

According to the theory of comparative advantage created by David Richardo, anything with utility must have an exchange value. A nation can then exchange its comparatively valuable things with others'. For being excellent comparatively, a nation must be excellent in technology. This will benefit the nation in involving in free trade since the use of technology can further accelerate production and enables the nation to compete internationally. As the consequence, the people in the nation will be more prosperous. (Dahlia et al., 2015). This theory gives emphasis on the importance of export and import for prosperity of a nation.

MSMEs IN INDONESIA AND THE CONTRIBUTION TO EXPORT

According to the Presidential Decree of the Republic of Indonesia number 99 year 1998, MSME is a type of business with net assets worth of maximum 200 million rupiah excluded buildings and land. More particularly, those classified as a small-scale enterprise are

those with net worth 50-500 million rupiah excluded buildings and land and sales income worth 300 million-2.5 billion rupiah. Meanwhile, medium-sized enterprise is a business with net assets worth of more than 500 million up to 10 billion rupiah excluded buildings and land and net sales worth of 2.5-50 billion rupiah (UU No 20 Tahun 2008 Tentang UMKM, 2008). Since they are small in scale, they therefore need to be protected.

MSMEs are the backbone of the Indonesian economy since they contribute 60.5% to the national gross domestic product and are able to absorb 96.6% of the workforce (*Google Scholar*, 2022). Nevertheless, their access to banking services is only 18% of 30% provided by the government (Ministry of Finance, 2022). Continuous supports must be addressed to them for maintaining or increasing their ability to give contribution to the national economy.

Many Indonesian MSMEs have been involved in exporting. Export is an activity to sell goods outside the customs area set according to the Customs Law (see figure 1 for the flow of exporting). Their export is in either raw goods, semi-finished goods or finished goods. Exporting raw goods means that MSMEs export materials originating from natural resources without processing them. Once the materials are processed into those needed as raw materials of other productions or supported domestic and imported materials, they involve in exporting semi-finished goods or finished goods. Generally, MSMEs are included in the exporting group if their export density is greater than 5%. Indonesian MSMEs' contribution to the national export is however still below 10%, which is lower than that of other developing countries (figure 2).

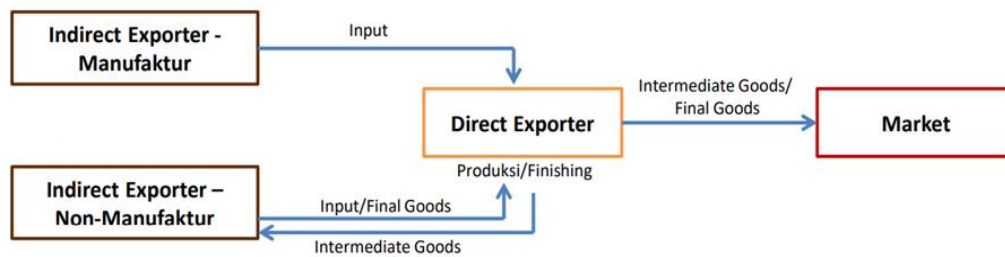


Figure 1. Export flow

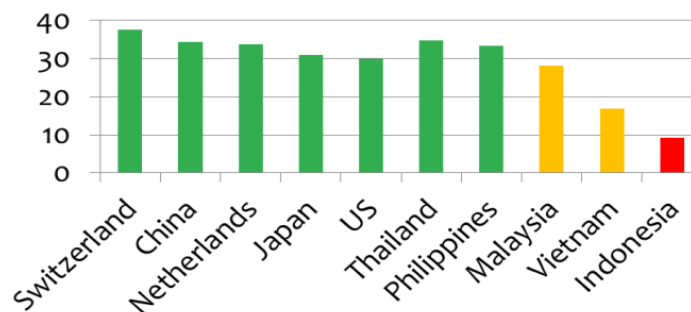


Figure 2. The Level of MSME Export Contribution

MSMEs have barriers to enter to the export market. The barriers the Indonesian MSMEs deal with are as follows:

1. Guaranteed supply chain of raw materials, raw goods and capital goods

Sustainability of export activities requires the guarantee of continuous supply of inputs, supporting materials and capital goods needed by MSMEs. Many MSMEs experience difficulties in getting this guarantee for their exporting. In other words, their exports are still low due to inadequate domestic supply chain. This brings consequences. For exporting, they need raw materials which some of them are imported. The data of the Indonesian Statistics indicate that imported raw materials have reach 75%. This is much higher than the import of capital materials which is approximately 16%. An increase in the price of the imported raw materials will eventually increase the price of the exported goods. Similarly, export by order

also requires continuity of raw materials, but suppliers of the raw materials are not always available widely.

Inadequate supply chain for raw materials, auxiliary materials, and capital goods is possibly the cause of low export level of Indonesian MSMEs. This brings MSMEs to face difficulty in finding raw materials with particular specifications.

2. Lack of legal knowledge

Indonesian MSMEs in general do not have sufficient knowledge of the legal requirements for doing an export such as the obligation to have tax identification number (NPWP) and business permits, knowledge on exports and imports restrictions.

The government provides convenient system for business licensing. Business licensing is done through The Coordination Body of Investment (BKPM) which currently launches a risk-based system called Risk-Based OSS, which is intended to simplify legal process. MSMEs with a low level of risk are required to have a business identification number (NIB) for a license. Those with medium risk must have NIB and Standard Certification Requirements (SS) in the form of an independent statement, while those with medium-high risk need to have NIB, SS verified by central/regional government agencies, and those with high risk need to have NIB, permits from the central/regional government, and relevant SS.

3. Access to finance

Indonesian MSMEs are still having difficulty to access financing from banks or other financial institutions. This is because banks apply high interest rates as the counter of lack of sufficient collateral experiencing by MSMEs. Long process for applying loans to financial institutions is another problem for MSME in getting the access.

4. MSME assistance

Indonesian MSMEs experience problems on improving product quality, product competitiveness, and managing the business. Assurances available for them in relation to these problems is currently still minimal.

5. Product quality

In fact, products manufactured by MSMEs have not yet met the standards and this reduces the bargaining power of the business.

6. Marketing

Limited knowledge about profitable markets, lack of understanding on market opportunities, and lack of understanding about promotional activities in particularly online marketing are the barriers of Indonesian MSMEs in exporting. Due to the advanced technology, the demand for online purchases through digital shops such as Shopee increases sharply during the post Covid-19 and currently there have been 180,000 MSMEs running the online shop. Shopee supports this issue by creating a slogan of getting 500,000 new exporters.

EMPOWERING MSMEs DURING THE COVID-19 PANDEMIC

Under the president Joko Widodo, the Indonesian government established a strategic policy for empowering MSMEs named the National Economic Recovery Program (PEN). The policy promoted the implementation of *Undang-Undang Cipta Kerja* (the Law Job Creation) and built national pride on local products known as *Bangga Buatan Indonesia* (BBI).

The PEN is a program formed by the government intended to strengthen and support MSMEs. The program launched *Kredit Usaha Rakyat* (KUR), a model of financial loan for MSMEs created to assist them to recover from the impact of the Covid-19 pandemic. The government also launched an assistance program for micro businesses called Micro Business

Productive Assistance (BPUM) which is to increase productivity of micro businesses that had possibly been so low due to the Covid-19 pandemic (Astuti A, 2022).

Another program created by the government is non-KUR interest/margin subsidies, a program that provide interest subsidies or margins for loans other than KUR. The government allocated funds for MSMEs and provide protection for credit made by MSMEs. The government also gives attention to cooperatives by financing the investments of cooperatives which carried out through LPDB KUMKM. It manages rotation of the funds of cooperatives, micro-level business, small and medium-level business.

During the Covid-19 pandemic, the government paid the final income tax (PPH) of MSMEs aimed at helping MSMEs to survive and develop their businesses against the pressure of the pandemic. Another effort undertaken by the government is to provide direct cash assistance to street vendors, entrepreneurs, small shop traders, and fishermen under the program called BTPKLWN. Social assistance provided to MSMEs with the above criteria helps entrepreneurs, small traders, and fishermen to pay bank installments. Workers deeply affected by the Covid-19 disaster were given assistance in wage by the government under the BSU program model. Unemployed people or those experienced layoffs due to the Covid-19 pandemic are given assistance through Pre-Employment Card that can be used in relation to developing knowledge or skills for looking better job. The government claims that the financial incentives for pre-employment people are the biggest incentives provided by the government compared to the other social assistances.

Referring to the 2020 data collected by the Indonesian Joint Funding Fintech Association (AFPI), MSMEs in Indonesia have reached 64 billion. However, 46.6 million of them do not have access to capital from either banks or other financial institutions. This phenomenon has prompted the government to support through other financing programs, such

as a partnership and environmental development program (PKBL), Mekaar PNM financing program, Micro Waqf Bank, Ultra Micro Financing (UMi), and credit for small businesses (KUR). These types of financing can be accessed by MSMEs according to their respective class levels and the types of levels of small businesses.

The governmental data indicates that credits made by MSMEs has continuously been growing by 16.75% and reached the amount of 1,275.03 trillion rupiah. Credit payment failures or bad loans (NPL) are steadily at 4%. The data indicates that the level of bad loans in 2022 was decreased. If the NPL in April 2022 was 4.38% or 0.38% higher than the standard NPL of 4%, but it was 4.41 % in the previous year.

President Joko Widodo sets the targets for MSMEs. Their exports must increase in 2024, their contribution is expected to increase to 17%, and as many as 30 million MSMEs reach the digitalization by 2024. MSMEs are expected not only to go digital but also to succeed in becoming global players whose orientation is to export.

The number of MSMEs in Indonesia have increased by 1.32% in 2021 or increased from 14.37% in 2020 to 15.69% in 2021. This brings opportunities for MSMEs to participate in the global market. They however must increase their competitiveness to strive the market by exploiting opportunities to integrate to the global market into GVC (Global Value Chain) and GEC (Global E-Commerce). Such integration can be carried out by conducting indirect export through local country aggregators or companies affiliated with the targeted countries.

Inevitably challenges for MSMEs to deal with are emerging new innovations and technology, developing digital literacy, increasing productivity, strengthening and understanding licensing or legalization of MSMEs, increasing access to financing, increasing creativity in branding and marketing, increasing capabilities of human resources, striving for

certification or standardization, increasing coaching and mentoring, providing training, as well as facilitating ability to grow.

CONCLUSION

Globalization must be able to bring more prosperity than harm to Indonesia. Empowering MSMEs can be to counter attack the impact of economic globalization that directs the world to become an oligopoly market and to be dominated by few. MSMEs in Indonesia are evidently unable to stem the impacts of economic globalization which is indicated by their contribution to export that is still below 10%.

The government has taken ways to empower MSMEs in Indonesia to reach the target of 17% contribution of MSMEs to the national economy. To leverage export of MSMEs, things to be done are to increase availability of supports, give assurance on continuity of supplies of raw goods, finished materials, capital goods, and provide easy access to financing.

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