

## SMEs Potential and Development towards Economic Growth in Indonesia

<sup>1</sup>Diwayana Putri Nasution, <sup>2</sup>Annisa Ilmi Faried

<sup>1,2</sup> Faculty of Social Science, Universitas Pembangunan Panca Budi, Medan, Indonesia  
Email: <sup>1</sup> diwayanaputri@dosen.pancabudi.ac.id, <sup>2</sup> annisailmi@dosen.pancabudi.ac.id

**Abstract:** The purpose of this study is to analyze the extent to which the potential and development of SMEs affect economic growth in Indonesia. This study looks at the effect of the number of business units and exports of SMEs on the value of GDP in Indonesia. This type of research is a descriptive study using secondary data. Secondary data used comes from data from the Ministry of Cooperatives and SMEs. This research also looks at how the potential and development of SMEs in Indonesia. This research shows that the potential of SMEs is very promising and overgrowing and providing positive economic growth for Indonesia. Small and Medium Enterprises have had a positive impact and are the backbone of the economy in Indonesia.

**Keywords:** economic growth, SMEs, potential, exports.

### 1. INTRODUCTION:

Sluggish economic growth is not only due to weakness in the commercial and financial sectors, but also due to the lack of strength in the structure of the economic sector in facing external or internal turmoil [1]. Before the crisis, the industry priority the government prioritized upstream industries and ignored the downstream industry. There is a kind of statement if the upstream industry is built, then the downstream industry will follow. However, in reality, the government ignored the concept of building a downstream industry that could be implemented [2]. Micro, Small, and Medium Enterprises (MSMEs) contribute significantly to economic growth. The Director General of Tax, Robert Pakpahan, said that MSMEs are the backbone of the economy. The number of MSME business units is 98.8% of the total business units in Indonesia. Absorption of its workforce is also relatively high, amounting to 96.99% of the total workforce. Moreover, accounts for 60.3% of the GDP. Supporting the development of MSMEs, the government reduced the amount of Income Tax (PPh) from 1% to 0.5%. The goal is not to burden small businesses and make it easier for them to continue to increase turnover.

Meanwhile, large industries that are built remain prone to these external shocks because they have a strong link in providing input. The delay in being promoted by SMEs in the program of building downstream industries and aligning the government with the development of substantial businesses results in a prominent role in large businesses. With the late promotion of the downstream industry, there was considerable disarray when the Asian crisis hit the economy. When a crisis occurs, large industries face severe problems while SMEs work according to their respective superior rhythms [3]. Two patterns of industrial growth are different because, among others, using raw materials from domestic sources, the use of labor with low wages and relatively fast moving towards adjusting raw material use and market-oriented. The above factors place SMEs able to show themselves to be businesses that have a competitive advantage and economic growth. Experts see the reality and argue that the process of economic recovery is supported by a significant increase in the role of SMEs. It shows that SMEs, besides being an antidote to the crisis, also has a very strategic role in the economy of a country. From the export side, we can see the development of SME exports from year to year according to the business scale as follows.

**Table 1.** Development of non-oil and gas exports according to business scale

Year	Value (billion rupiah)				
	SB	MB	SME	LB	Total
2002	20,496 (5.13)	66,821 (16.74)	87,290 (21.87)	311,916 (78.13)	399,206 (100.00)
2003	19,941 (5.21)	57,156 (14.94)	77,097 (20.15)	305,437 (79.85)	382,534 (100.00)
2004	24,408 (5.18)	71,140 (15.11)	95,548 (20.30)	375,242 (79.70)	470,790 (100.00)
2005	27,700 (4.86)	81,429 (14.30)	109,129 (19.16)	460,460 (80.84)	569,588 (100.00)

SMEs also contribute to export revenues, although the contribution of SMEs is much smaller compared to the contribution of large businesses. In 2005 the value of small business exports reached 27,700 billion and created a role of 4.86 percent of total exports. Whereas in 2002 the export value of the same business scale amounted to 20,496 billion and created a role of 5.13% of total exports. It means that there is an increase in value even though the role of exports in small businesses has decreased slightly. For medium-sized businesses, the value of exports also increased from 66.821 billion in 2002 (16.74%) up to 81,429 billion with a declining role of 14.30% in 2005. Based on the distribution of export income according to business scale, the 2003-2005 period of the largest export driving sector is the processing industry, and the smallest export contributor is the sector of agriculture, livestock, forestry, and fisheries. Especially for small businesses, the most significant contributor to non-oil and gas exports is the manufacturing industry sector, which is followed by agriculture, livestock, forestry, and fisheries, and finally the mining and quarrying sector. Whereas for medium enterprises, the most significant contribution to exports is the manufacturing sector. The role of Small and Medium Enterprises (SMEs) in Indonesia is huge and has been proven to save the nation's economy when the 1997 economic crisis hit it. In advanced countries, both in the United States, Japan, Germany, Italy, it is the central pillar of the country's economy. Also, efforts to develop SMEs by synergizing with large industries through partnership patterns will strengthen the economic structure both nationally and regionally. The participation of related parties or stakeholders needs to be continually developed so that SMEs can genuinely be able to take a more significant role in the national economy.

## 2. THEORIES:

### 2.1 Economic Growth

Economic growth is a process of changing the economic condition of a sustainable country towards a better condition for a specified period [4]–[6] Economic growth means the development of activities in the economy, which causes the goods and services produced in society to increase, and the prosperity of the community increases [7]. So that economic growth can also be interpreted as a process of increasing the production capacity of an economy that is realized in the form of an increase in national income. Their economic growth is an indication of the success of economic development. The theory is built on practical experience, so that theory can be used as a basis for predicting and making policies. In general, the theory of economic growth, according to experts, can be divided into 2, such as the historical economic growth theory and the theory of classical and neoclassical economic growth [8].

### 2.2 Small and Medium Enterprises (SMEs)

The reasons for SMEs to survive and tend to increase in number during the crisis are:

1. Most SMEs produce consumer goods and services with an elasticity of demand for low income, so the average level of income of the community does not have much effect on the demand for goods produced. Conversely, the increase in income level also does not affect demand.
2. Most SMEs do not get capital from banks. The implication is the deterioration of the banking sector and rising interest rates, not much affecting this sector. In contrast to the problematic banking sector, SMEs are also affected by their business activities. While large periodic businesses can survive. In Indonesia, SMEs use their capital from savings, and access to banking is very low.

SMEs have limited capital and competing markets, the impact of which is that SMEs specialize in tight production. It allows SMEs to move from one business to another quickly; the entry and exit barriers do not exist. Reforms eliminate barriers in the market; upstream industrial protection is eliminated, SMEs have more choices in the procurement of raw materials. As a result, production costs fall, and efficiency increases. However, because it coincided with the economic crisis, the effect was not too significant. The existence of a prolonged economic crisis caused the formal sector to lay off many workers. The unemployed enter the informal sector, generally conducting small-scale business activities. As a result, the number of SMEs is increasing.

### 2.3 SME Exports

Export is the process of transporting goods or commodities from one country to another. This process is often used by companies with small to medium business scale as the primary strategy to compete at the international level [9]. The export strategy is used because of the lower risk; capital is smaller and more accessible when compared to other strategies. SMEs in Indonesia is highly expected because they have great potential as one of the relevant sources of development (diversification) and growth in X, especially X manufacturing. The ability of Indonesian SMEs to realize their potential X is determined by a combination of several factors of the relative advantages that Indonesian SMEs possess over their competitors, both from within large businesses and abroad [10].

### 3. METHODOLOGY:

The material in this study uses descriptive material with a qualitative approach. By explaining the potential of SMEs and their development in Indonesia through research and literature studies, to make a precise, factual, and accurate enunciation of the facts and nature of a particular population or area. Who will later find a model of SME product development in Indonesia? The research was conducted in several stages, such as the preliminary stage, reducing the data, presenting the data, presenting the model, and drawing conclusions, according to the following:

- The preliminary stage is carried out by carrying out preliminary observations, finding the phenomenon of the problem and identifying the initial problem in the research and making a research proposal.
- The second stage is the stage of reducing data by process of synthetic thinking that requires intelligence and breadth and high depth of insight. While reducing data means summarizing, choosing the main things, focusing on the things that are important to look.
- The third stage is the presentation phase of the data; the presentation of data can be done in a brief description, chart, relationships between categories, flowcharts, and the like. The presentation of data carried out by the author is data from library studies and previous research related to the topic of discussion
- The fourth stage is the presentation of the model by interpreting the results and comparing the results of previous studies.

### 4. RESULT AND DISCUSSION:

#### 4.1 Development of SMEs

Micro, small and medium enterprises (MSMEs) have a vital role in the development and economic growth, not only in developing countries such as Indonesia but also in developed countries. In Indonesia, the role of MSMEs in addition to playing a role in the development and economic growth, MSMEs also have a critical role in overcoming the problem of unemployment. The growth of micro-enterprises makes it a source of growth in employment and income. By absorbing much labor, MSMEs also have a strategic role in the government's efforts to fight poverty and unemployment.

The contribution of the micro, small, and medium enterprises sector to gross domestic product increased from 57.84% to 60.34% in the last five years. Uptake of labor in this sector also increased from 96.99% to 97.22% in the same period.

#### 4.2 Export Request

The export of SMEs in Indonesia has increased quite rapidly. Of course, this is an opportunity for domestic business actors. One example that can be seen is the export of halal products to the UKM sector. Indonesia, as the largest Muslim population in the world, has an auspicious opportunity. Also supported at this time, the demand for products globally continues to increase. For the Southeast Asian market, exports of halal products reach 100 million dollars. This number has increased by 100% compared to the previous year, which only reached 50 million dollars. The need for halal products, not only in the Arab country or with the majority Muslim population but seems to have become the lifestyle and needs of the world community. The halal food product market, which is the central business portion of the world, is in Muslim majority countries such as Algeria, Bahrain, Egypt, Indonesia, Iran, Iraq, Jordan, Kuwait, Lebanon, Yemen, Malaysia, Morocco, Oman, Qatar, Syria, Saudi Arabia, Tunisia, Turkey and the United Arab Emirates. Some of the capital to seize the world halal product market, in principle, is already owned by domestic businesses, one of which is formal legal (halal certificate) to produce and distribute unlimited halal products. Only for food and beverage products, in this case, Indonesia has an MUI whose legal fatwa, and the world has recognized the certificate. Coupled with the passing of the Halal Product Guarantee Act. According to data from the Brand Research Institute, Inc., other Asian countries that have the potential to become export destinations for Indonesian halal food products are Malaysia. However, unfortunately, until now, Indonesia is still ranked fourth after Australia, China, and New Zealand in terms of exporting halal food and beverage products to Malaysia. Even though Indonesia is very likely to market halal food and beverage products in Malaysia because halal authorities have recognized the halal certification issued by the Indonesian Ulema Council (MUI) in Malaysia. Other countries that are targeted to become Indonesia's export destinations are OIC countries. In the food sector, especially commodities of meat and live animal, OIC countries annually import these commodities at 15.4 billion US dollars each year. 91% of these imports come from countries that are not affiliated with the OIC while in the European Union, despite the population Muslims are a minority and the number is small, the growth in demand for halal products, especially food and beverages is quite significant due to high purchasing power, such as in France and the Netherlands. In France, residents spend 30% of their income on halal food. The quantity of meat food consumption is around 400 thousand metric tons a year. "Diversity Baby-Boomers Du Halal" or the era of birth of halal product variations began in 2009 marked by the rise of halal food products launched, not only by small entrepreneurs, such as meat sellers, but also French national companies, such as Fleury Michon, Herta, Knorr, Labeyrie, Liebig, and

Maggi. For Indonesia, it is estimated that there will be an increase in demand for halal meat food products reaching 1.3 million metric tons a year. The enormous potential of the world's halal product industry is an opportunity and challenge for the country of Indonesia. It is an opportunity because Indonesia has capital both human resources, natural resources, and supporting institutions for halal products. In this case, MUI and some formal legal regulations already exist, so that domestic businesses can take advantage of all of them to capture the opportunity for the halal product industry to become a challenge because along with the large share market in the halal product industry, other countries also dedicate and prepare themselves to become halal products producers world. If Indonesia is not able to develop halal products, then Indonesia will forever be the market for halal products for exporters of halal products. Therefore, cooperation between the stakeholders of the halal product industry is needed, starting from the government, institutions related to halal products, SME business people, and the general public. The development of halal products also ultimately affected the export of SME products in Indonesia.

### **Potential of SMEs towards Economic Growth**

The relatively high household consumption sector is beneficial to slow down the impact of the weakening global economy, but the State cannot rely on these two sectors in the long run. Breakthroughs in the economic field ideally should be done to increase economic growth. Based on BPS data, 99.9% of business units operating in Indonesia are MSME-type business units. This potential is relatively large, and if managed properly, it will make a positive contribution to the Indonesian economy. However, such a large number does not guarantee a significant contribution to the economy. Until now, the MSME sector was only able to contribute to GDP by 61%. Most entrepreneurs, especially those engaged in the micro business sector, are still below the poverty line. They are only able to run a business to survive. On the other hand, after the 1997-1998 crisis, the MSME sector can play a role in economic growth and employment. It has an impact on Indonesia's resilience that can stand when, globally, the world experiences an economic slowdown.

Citing data from the Ministry of Cooperatives and SMEs, currently, the number of SMEs in Indonesia reaches around 57 million business units. It is the amount recorded by the government; the amount can be more with scattered and not yet integrated data. Indonesia's MSMEs currently only have access to the global supply chain of 0.8%. Many MSMEs who enter the sector are unplanned because the formal sector does not absorb them, so the government's role in the development of MSMEs is necessary. This sector is a sector that will remain promising as long as the population continues to grow. MSMEs generally have weaknesses in access to finance and technology. It causes enormous inequality in small businesses and large businesses. Currently, large businesses account for only 0.7 percent of businesses in Indonesia, but have an added value of 89 percent, while small businesses with a total value of 99 percent are only five percent so that it is difficult for MSMEs to dominate the market due to the difficulty of access.

The Canadian Finance Minister plans to close the tax gap for small businesses that have excellent performance. Meanwhile, Finance Minister Sri Mulyani applied an SME tax of 1% which was reduced to 0.5%. (PP 23 of 2017). It is a significant first step; in the future, the government should immediately improve the quality of policies that support the creation of a conducive atmosphere for MSMEs to grow steadily. It has an impact on economic growth in its objectives. The increase in SME units will increase people's income and also increase public consumption so that the value of GDP increases, which leads to increased economic growth.

### **5. CONCLUSION:**

This study concludes that the potential and development of SMEs is enormous and has been supported by the Indonesian government with policies that promote the SME sector in Indonesia. The competitiveness of our SME products is also excellent so that it can participate in the global competition in a world characterized by an increase in the value of export of local product trends in the international arena. The government can focus more on developing the existing SME sector because there are still many opportunities that have not been optimally explored. Examples of capital lending, training, and technology improvements. This factor is useful and has a strategic effect in overcoming the problem of unemployment and economic growth. By increasing the role of the SME sector through training and funding assistance, it can ultimately improve the welfare of the community in particular and Indonesia's economic growth in general.

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