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Risk-shifting in anticipation of the trade liberalization effect of MSMEs

ABSTRACT

The focus of MSME studies during the 1998 crisis in Indonesia was on resilience. Now, MSMEs are using debt higher as financing for business development to face the trade liberalization effect. Their behavior is based on the risk-shifting hypothesis (Jensen & Meckling, 1976), which will transfer risk to debtholders, in the event of financial difficulties. This high debt does not reduce investment for business development (under-investment) (Myers, 1977), but vice versa.

Keywords: Risk-shifting, Trade liberalization, MSMEs

INTRODUCTION

The sudden presence of the crisis in Indonesia in 1998 was due to political factors, political instability during Suharto's presidency, the succession of the coming government, and opposition repression (Saidi, 2008). This situation has an impact on the decline in domestic demand and the depreciation of the rupiah, which has an impact on the survival of all industrial sectors (Thee, 2000). However, MSMEs still survive, because they are too large because of the low dependence on imported raw materials. So that currently what makes the challenge for MSMEs is no longer a crisis but is the trade liberalization effect (Tambunan, 2009).

MSMEs have a strategic position because, based on data (KemenkopUKM, 2016, 2018) it is carried out by the majority of Indonesians, the number of businesses is more than large businesses, the contribution to GDP is large (Martono et al., 2020). The ability to absorb labor has increased as well as an increase in the number of exports from the 2010 - 2018 period. However, the exportability of MSMEs is not yet comparable to large businesses, even though it has great potential. In 2018, on average, each MSME was only able to export 0.31% of total exports. This situation motivates us to know the description of financial factors, production, marketing, and human resources to find out the position of opportunities and threats of trade liberalization.

We find that the liberalization effect has an impact on increasing production both with imported and local products. This situation encourages MSMEs to develop businesses with debt as the main instrument in financing even though they have limited asset guarantees. So they tend to do risk-shifting (Jensen & Meckling, 1976), if business development is successful then enjoy being with debtholders, but if it fails, debtholders also bear the risk.

Therefore section 2 describes MSMEs in Indonesia, section 3 describes the sample data of MSMEs. Furthermore, section 4 about the findings and discussion. Finally, section 5 is the conclusion.

MSMEs in Indonesia

Whereas the understanding of MSMEs on Micro, Small and Medium Enterprises sets limits on the MSME criteria as follows (UU No. 20, 2008)

1 The criteria for Micro Business are as follows: (a) Has a net asset of no more than Rp 50,000,000 (fifty million rupiah) excluding land and buildings where the business is located, or (b) Has annual sales results of at most Rp.300,000,000.00 (three hundred million rupiah).

Small Business Criteria are as follows: (a) Has a net worth of more than Rp.50,000,000.00 (fifty million rupiah) up to a maximum of Rp500,000,000.00 (five hundred million rupiah) excluding land and buildings where the business is located, or (b) Has annual sales results of more than Rp.300,000,000.00 (three hundred million rupiah) up to a maximum of Rp2,500,000,000.00 (two billion five hundred million rupiah).

The criteria for Medium Enterprises are as follows: (a) Has a net asset of more than Rp. 500,000,000.00 (five hundred million rupiah) up to a maximum of Rp 10,000,000,000.00 (ten billion rupiah) excluding land and buildings where the business is located; or (b) Has annual sales results of more than Rp2,500,000,000.00 (two billion five hundred million rupiah) up to a maximum of Rp50,000,000,000.00 (fifty billion rupiah).

Nicolescu (2009) describes the characteristics of the competitiveness of MSMEs in the global era depending on internal and external factors. External factors such as culture, people's purchasing power, and the level of competition due to macroeconomic conditions. In addition, it is also caused by internal factors, namely company size, stakeholders, educational background (Sari et al., 2015).

METHOD

Based on the type of business, they can be grouped into 5 types of industry and most of them are in the food and beverage sector. Most of the food and beverage sector is also on a micro-scale because it is done by households and usually has a relationship with the founder if it is done not the founder.

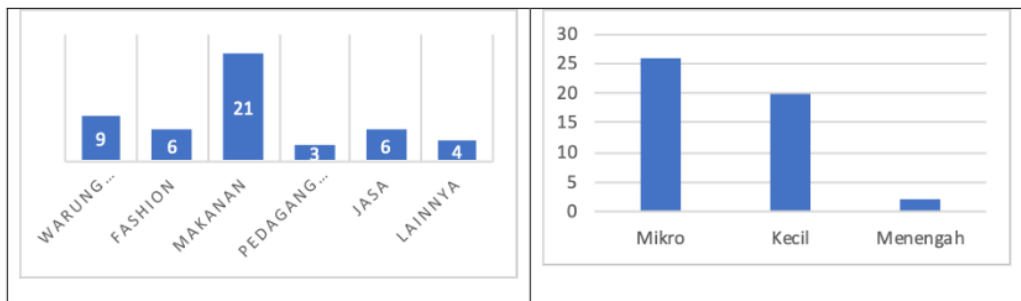


Fig.1: Types of Industry

RESULTS AND DISCUSSION

Management Factors

This study shows that the general factors composing the inability to manage the business are caused by several factors as shown in Table 4.1. These factors can be divided into two elements, namely the ability to manage the organization and the background of the founder of the business. The table shows that the largest component value is an indicator that the owner is not able to control the risk. This indicates that the owner's inability can trigger the business not to last long. Therefore, the lender needs to pay close attention to the ability of the owner to be able to control the risks he has. When the owner is unable to control the amount of his debt so that he has too large a debt burden or too large operating expenses, it

can indicate that the risk of the business is too great to obtain new debt (Cultrera & Brédart, 2016).

The creditor should be careful with small businesses that have a large risk, another component, namely the inability of the owner to cooperate with other parties and make decisions, this indicates that bad cooperation between the business and other fields can reduce the number of sales and the risks will become bigger because the owner is unable to cooperate with other people to run the business. If a business can cooperate with other business owners so that they can complement each other to get income, this indicates an acceptable income in the future so that it can reduce the risk of failure to pay. The second factor that also affects the owner's failure to predict risk is the difference in understanding between the owner and the employee so that things like this can be mitigated by the lender, but this risk is not as big as the owner's inability to predict future risks.

Marketing

that the orientation of MSMEs does not always prioritize consumers and does not pay attention to market research, it is necessary to observe further if otherwise MSMEs can adapt and meet consumer tastes, they can be given leeway for providing credit because there is a potential that they can pay debts on time and their capabilities are quite reliable.

Production

Production is closely related to the products owned by the business, if the business has only one product, it can provide insight that if there is a decrease in demand, the business is unable to have other income so that it can indicate a decrease in profits and income (Ciliberto & Schenone, 2012). Based on the results of the research, it shows that businesses need to pay attention to news or information related to economic development, this indicator shows the greatest value as a factor that affects the production of a business in the current era where the corona pandemic occurs in the information reported by the mass media, it is quite clear that it happened. the decline in demand for MSME products so that they experience a blow to demand because the amount desired by consumers is not too much.

Finance

Management factors are closely related to one's ability to control expertise in the financial sector, someone who is an expert is said to be able to plan well the aspects of income and expenses so that he can have a business plan (Falkner & Hiebl, 2015). A business owner who is able to balance expenses with income will be able to maintain the business for a long enough time because the expense of expenses can be balanced with income, it would be better if the expenditure is less when compared to income so that it has advantages that can be used to maintain business continuity in terms of factors. Income.

External

more competitors, it can become a business obstacle to obtain sufficient profits so that it can reduce the ability of MSMEs to pay debts (Matias & Serrasqueiro, 2017). The fewer competitors, the greater the potential for the income they have due to the limited number of products and not many other businesses that have similar products.

Threats and Opportunities to face the Trade Liberalization Effect

Switzerland, Germany, and Italy use cluster development strategies to boost the MSME sector. The strategy begins with the identification of existing clusters that have the potential to become strategic industries. This can be seen in the metal and machinery industry sector in Germany and the formation of high technology industrial clusters (agglomerations)

in Silicon Valley, United States. The development of industrial clusters encourages the concentration of several companies which in turn form inter-firm networks in the use of technology, increase inter-industry linkages, and decrease product marketing costs. This, in turn, encourages the achievement of economies of scale in the use of inputs, technology, and marketing (Sari et al., 2015)

However, the phenomenon of business ownership in Indonesia is concentrated and the existence of controlling shareholders who have family relationships (Claessens et al., 2000; La Porta et al., 1999), so they tend to maintain networks between entrepreneurs. They will try to maintain control over the company, thereby reducing foreign intervention. Many MSME actors whose businesses are carried out from generation to generation and have survived the crisis. However, they are not oriented towards exports which are too large because they only fulfill domestic products.

Because they operate in domestic products so that their production capacity is relatively stable and the business competition factor is relatively high. Business actors think that their starting point of the strategy is capital. With capital, they can reduce business competition through product innovation, both on differentiation and diversification.

Agency problem between agent and principal (Jensen & Meckling, 1976), does not occur because the functions of ownership and control are managed-owned. The owner-manager tries to protect his interest in doing business because it is the only source of income. However, an interesting thing was found, namely that MSME entrepreneurs are dependent on debt even though there are limited fixed assets as collateral.

The implication of dependence on debt results in an overhang (Myers, 1977), MSMEs will lose growth opportunities. The decision to invest in MSMEs for business development is limited to debt financing so that when it is excessive it becomes an overhang. Entrepreneurs will reject business development investment when it is felt that it only benefits debtholders without providing significant benefits to entrepreneurs (underinvestment hypothesis). Debt will become "tax", because the income is first used to pay debt and loan interest.

CONCLUSION

MSMEs in Indonesia have a family ownership structure with unique characteristics, namely dependence on debt for financing and business development. However, with the high business competition, they do not reduce debt and tend to do risk-shifting (Jensen & Meckling, 1976). They choose projects with high risk in developing MSMEs, even though they use debt so that if the project fails, the debtholders also bear the risk.

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