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ROLES OF MICROFINANCE INSTITUTIONS FOR SUSTAINABILITY OF MICRO ENTREPRENEURS IN INDONESIA

[1]Yohana F. Cahya Palupi Meilani, [2*]Sabrina O. Sihombing, [3]Budi Hartono Kusuma

Lecturer of Universitas Pelita Harapan, Tangerang, INDONESIA

**Corresponding Author: Sabrina O. Sihombing*

Abstract: **The purpose of this article is to provide an overview of the roles of microfinance institutions in relationship for sustainability of the micro entrepreneurs in Indonesia. Specifically, this paper aims to develop a conceptual framework predicting the relationship of the role of microfinance to the sustainability of micro entrepreneurs. Micro finance institutions in Indonesia play an active role in contributing to micro financing activities. These roles are performed as a manifestation of Law Number 1 year 2013 on micro finance institutions. The presentation of this article is divided into the following formats: (1) the history of microfinance institutions in Indonesia, (2) the conceptual definition of microfinance institutions, (3) the exposure of the implementation of Law Number 1 year 2013, (4) Form the current of micro finance institutions, (5) the roles of micro finance institutions for sustainability of micro entrepreneurs. By Law number 1 year 2013 on micro finance institutions in Indonesia today supports micro business actors in maintaining business and business development in the future. The contribution of this article helps provide an overview for the parties related to the management of microfinance institutions and micro business actors to support the growth of the micro entrepreneurs in Indonesia. Instead that, the purpose of micro finance institution is not only to seek profit, but also to increase the income and welfare of the people and to help increase the economic empowerment and productivity of society.**

Keywords: **Microfinance Institution, Micro Entrepreneurs, Sustainability.**

I. INTRODUCTION

Many Indonesians are still low-income people, who lead them to live below the poverty line. With such a complicated condition, it is necessary an institution that can hold them to improve the standard of living, especially in improving economic conditions. Based on Indonesia Central Bureau of Statistics (BPS), the number of poor people (population with per capita expenditure per month under the Poverty Line) in Indonesia as of September 2016 reached 27.76 million people (10.70 % of total population). Poverty refers to a condition the powerlessness of a society in a system of government causing society to be on oppressed position. So that poverty in the form of lifestyle, culture, interaction created because of the role of that structure oppress (Miranti, 2010). Haughton and Khandker (2009) stated that poverty based on World Bank definition is the lack of prosperity. Based on this, then the question arises about what is meant by welfare and what is the point of departure to measure it. One of the approaches used is to assume welfare as a mastery of goods in general, so that society can become much better if they have greater control over resources.

Then micro and medium enterprises in Indonesia often associated with problems economic and social conditions such as high poverty levels; inequality income distribution; which development process uneven between urban and rural areas; as well as problems of urbanization. Criteria of small and medium enterprises according the Law Number 20 Year 2008 on Small and Medium Enterprises, that small and medium enterprises are classified by total assets and turnover owned by a business. That belonging to a micro enterprise (business with maximum assets of 50 million and sales maximum 300 million). The developments of micro and medium enterprises are expected to provide a significant positive contribution to

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countermeasures problems mentioned above (www. bi.go.id, 2015). From the point of view of employment, micro, small and medium enterprises provide a very significant contribution to the creation of employment (Yahaya et al., 2016; Bouzza, 2015). Related with Yoseva and Teuku Syarif (2010) that stated in Indonesia, most of the micro business actors, especially those engaged in the agricultural sector and informal sector, have net income of less than USD 1,440 per family per year. Still belonging to the poor because earning less than USD 1 per person per day. Approximately 89 million workers or identical to 96.7% of the workforce in the business world is dominated by micro business actors.

The result of research and survey conducted by BPS (2014) is that the most dominant factor of problem faced by micro business enterprise is access to capital. For those conditions, it takes a financial institution that can be present in the community to help stabilize economic conditions. The institution is a financial institution capable of providing services in the form of services to people who have minimal income and enter the poor circle. In addition, it can helps small and micro entrepreneurs who still need help in the business. Forms of assistance can include loans, micro business financing and savings management. Even in the last two decades there has been a significant increase in the diversity of institutions providing financial services to the needy poor (Fernando, 2008).

There are various micro finance institutions service platforms in Indonesia. This is done as community empowerment, especially lower middle income and micro, small and medium enterprises. In the specific, micro entrepreneurs are those who need comprehensive support from financial institutions. This matter mapping, monitoring and the evaluation of financial services is more complex. Overlapping rules, authority and scope extensive services of microfinance institutions also participate contribute to the difficulty of applying the right development strategy. Sakti (2013) stated that in the Indonesian economy there are 51.2 million units or 99.9% of business actors dominated by micro and small business units.

Micro finance institution serves as an intermediary institution, both profit (profit motive), and social (social motive) for society development (Baskara, 2013). Some challenges possessed by micro business that has been factors inhibit the competitiveness of micro entrepreneurs against larger scale of business are financial. The problem according BPS (2016), if micro entrepreneurs are not empowered, can causing greater poverty and burdening entire nation. But when micro entrepreneur is empowered properly, will be develops into a medium-sized business. Especially in Indonesia context, the role of micro finance institutions means supporting the conception of the people's economy. Community economy is a solid business partnership among all actors of economic life with the principle of mutual benefit. With the realization of a solid business partnership is expected economic activity, especially can grow stronger. Financial services institutions such as micro finance institution is basically indispensable to support development activities the rural economy. It is primarily as facilitation institution of financing services for micro and small business actors. The reason because that micro business actors are generally struggling in capital problem. On the other side, the formal institutions such as banks are often inaccessible by micro business actors. Due to various factors such as banks requirements in the application of business capital credit.

Therefore, it is the need literature-based understanding of the roles of microfinance institutions for sustainability or micro entrepreneurs in Indonesia context. In this conceptual article will be presented history of microfinance institutions in Indonesia, including a review of the conceptual definition of microfinance institutions. This exposure will be able to adding to our understanding of existence this institution as well as the various obstacles it faces. Includes exposure the implementation of Law Number 1 Year 2013 The discussion concludes with a related study of the role of micro finance institutions to build ability of micro entrepreneurs to maintain business.

II. LITERATURES REVIEW

History of Micro Financial Institution in Indonesia:

The role of the Indonesian government in the development of microcredit during the Old Order era of 1945-1965 was not much. In these times there were political upheaval as well as the Republic Indonesia experienced wartime retention independence. In the period 1957 to 1965, the formal financial system is strongly restrained. There are policies that remove everything ownership of foreigners within the banking system used to belong to the Netherlands (Baskara, 2013).

In the New Order era of 1966-1998, after starting stable political conditions, government began pay great attention to development rural. In the early 1970s the government established a bank in every provinces which. The government also delivers flexibility in establishing Rural Banks. There are approximately 300 Rural Banks throughout Indonesia (Arsyad,

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2008; Baskara, 2013). It means, at that time these institutions were treated as a non-bank financial institution, and based on the Banking Act of the Year 1967 does not meet the requirement to obtain liquidity credit from Bank Indonesia, and by therefore funds from this institution should be collected from other sources. These institutions are also not allowed to mobilize funds in the form of savings and not tied to the interest rate rule of Bank Indonesia, set their own interest rate (Arsyad, 2008).

A significant change occurred at 1988; the government set several types of nonbank financial institutions. Nonbank financial institution is given opportunity for two years become a Rural Bank. This regulation is quite difficult for financial institutions, and then later government decided to delete the rule above. Then period the late 1990s are also marked by many the emergence of commercial banks that do specialize his efforts on the micro segment. In early 2000, the government through the relevant ministries established a forum called the Joint Movement of Microfinance Development Indonesia.

In early 2000, the government through ministries established forum Joint Movement of Micro finance Development Indonesia. In 2001, Bank Indonesia submitted the draft bill on micro finance Institutions to the Minister of Finance. Then Bank Indonesia forwarded it to the House of Representatives to be ratified. But there is no sign of the House of Representatives to immediately pass the rules. Bank Indonesia in 2003 together with Promotion of Small Financial Institution (Pro-Fi) from German, issued a study and formulation on the management and development of micro finance. The study suggests the government to eliminate everything that hinders the development of micro finance institutions and drafting and issuing legislation. Specifically regulates the existence and management of micro finance institutions. Finally in 2010, the Draft Law on Micro finance Institutions was ratified. Then however, many micro finance Institutions are not yet legal entities and have business licenses. So the draft law of micro finance in order to provide a strong legal basis for the operation, on January 8, 2013 has been enacted by Law Number 1 Year 2013 on micro finance institutions.

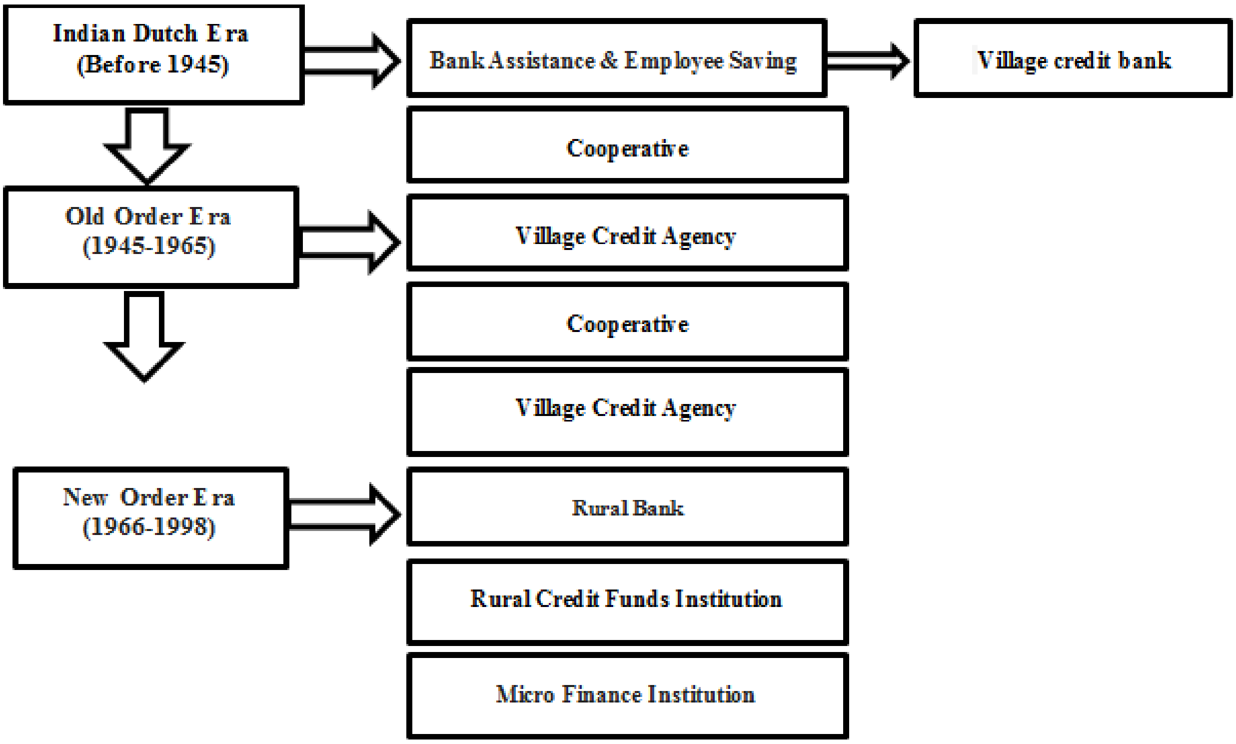

Fig 1: Scheme of History Micro Finance Institutions Forms in Indonesia

Conceptual Definition of Microfinance Institutions:

Micro finance institution is an institution that providing financial services to the lower income people and included in the poor society. Micro finance institution brings the demand for the funds of the poor over availability of funds. For formal banking financial institutions, poor people difficult to be served because of the requirements. Associated with poverty reduction efforts, micro finance institution has a strategic meaning. Seen from this perspective of strengthening micro entrepreneur and play a role in two channels. First, micro entrepreneur can create job opportunities, relatively labor-intensive with little capital. Secondly, through development micro businesses that is directly linked to the poor to have productive enterprise (Arsyad, 2008). Bank Indonesia defined micro financial institution is institution that given credit to the perpetrators productive both individuals and groups that have sales results below one hundred million rupiah per year. Asian Development Bank (ADB) defines a micro finance institution as an institution providing depository services, credit (loan), various payments transaction services (payment services) and money transfer intended for the poor and small businesses (Susilo, 2007).

Microfinance Institutions can be distinguished from the following values: (1) Justice, provide equal opportunities to the community, especially the poor or low income people to get services from the micro finance institutions. (2)Togetherness, activities undertaken jointly for the common good. (3)Independence, an activity that is carried out without much depends on other parties, both from the aspect of human resources and capital. (4)Ease, the financing and depository procedures in the micro finance institutions are made as simple as possible. (5)Openness, a business activity whose management process can be known by the community. (6)Equity: lending and financing that reaches all poor and / or low-income people. (7)Sustainability: an ongoing and continuous undertaking that is not limited by time (Susilo, 2007).

Micro finance Institutions are established to provide business development services and community empowerment, either through loans or financing in micro-scale enterprises to members and communities, savings management, or the provision of business development consulting services that do not merely seek profit (ojk.go.id, 2016). Then Law Number 1 Year 2013 defined micro finance institution is a Financial Institution with legal status, owning capital and obtaining business license. The form of legal entity may be in the form of a cooperative or a limited liability company.

Based on the Law 1 Year 2013, the requirement to create a micro finance institution is not difficult, namely: Indonesian citizen; Village-Owned Enterprises; Cooperative; District or Local Government. Prior to running a business, the micro finance institutions must have a business license from Financial Services Authority (OJK). Micro finance institutions business permit is divided into 2 (two), namely:

1. Application for new micro finance institutions license since the micro finance institutions act valid (established since January 8, 2015).

2. Application of micro finance institutions license through inauguration, for micro finance institutions that have been established and operates before the Act takes effect (has been established and operated before January 8, 2015).

Exposure to Implementation of Law No.1 of 2013:

Based on article 33 Paragraph (1) Year 1945 Republic Indonesia Constitution stated that the economy is constituted as a joint effort on the principle of kinship. In a broader sense, it is formulated in paragraph (4) of the aforementioned article that the national economy is organized on the basis of economic democracy with the principle of togetherness, efficiency, justice, sustainability, environmental insight, independence, and by maintaining a balance of progress and national economic unity. Micro finance institutions are referred to as implementers of that populist economy. Referring to Law Number 1 Year 2013 on micro finance institution, this institution is a nonbank institution that is part of the national economic arrangement. This means that in its activities micro finance institution taking part in the achievement of a prosperous economic life. Both for those who are members of the association itself and for the customer and the surrounding community. Micro finance institution as associations specifically established to provide business development services and community empowerment, either through loans or financing in micro-scale enterprises to members and communities, savings management, as well as providing consultancy services in developing businesses that are not solely for profit.

Implementation of Law Number 1 Year 2013 since two years after its enactment. That the application for a business license to the Financial Services Authority must be done by the micro finance institution that already operate within one year of this rule invited. This is done to give a grace period for micro finance institutions to adapt their activities with applicable rules. All things which have not been governed by this rule, including the problem capital, management, and others will be regulated through regulatory authority of financial services (Baskara, 2013).

Government Regulation Number 89 Year 2014 on Interest Rate of Loan or Return on Financing and Area Coverage of Business Area of Micro Finance Institution as the implementation of Law Number 1 Year 2013. This means that the

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Financial Services Authority continues to encourage the interest rates provided by microfinance institutions to be lower in order to improve the level of welfare of Indonesian society, especially the people who are in the lower class. This is related to efforts to minimize the practice of loan sharks to micro business actors. And in the implementation of control to microfinance institutions are required to report the maximum interest rate of the loan or the maximum yield of financing to the authority every four months. The capital of the micro finance institution consists of paid up capital for the legal entity of limited company, while the legal entity of the cooperative, the capital consists of principal savings, mandatory deposits and grants.

Form the current Microfinance Institutions:

Given that micro finance institutions are not only become lenders of capital but also collect excess funds owned by the community. So that micro finance institutions the must be licensed and incorporated. Like the Financial Services Authority discourse that obliges the micro finance institutions to be legal until the period of January 8, 2016. If until such time limit has not obtained business license from Financial Services Authority, it is considered as illegal micro finance institutions. Therefore, Financial Services Authority facilitates the licensing process. This reduces the concerns of micro business actors who transact, into legal status owned by the micro finance institutions, since it has been mentioned earlier that in Indonesia there are still many unlicensed micro finance institutions.

There are four forms of micro financial institution: (1) formal form such as banks and non-banks, such as rural bank and cooperative that existed before Indonesia became independent, (2) non-formal form which incorporated and not legal entity, (3) A program government, (4) form is informal such as loan sharks. While the Bank Indonesia only divides the two categories i.e. micro financial institution in the form of People Credits Banks or Non-Bank such as Cooperative (Yahaya and Usman, 2009). Cooperative (*Koperasi*, in Indonesian language) is a business entity based on kinship and togetherness. Then Baskara (2013) divided into two, formal and informal. The fundamental difference between the micro finance institutions is because formal micro finance institutions have legal entities, while informal micro finance institutions come from private or non-legal groups. Formal micro finance institutions consist of banks that are People Credit Banks and conventional banks that specialize in business loans such as Micro Units, Savings and Loans, and others, not banks such as cooperatives. While informal micro finance institutions are NGOs, moneylenders and the activities of collecting money or goods of equal value by some of the guides called *arisan*.

Micro financial institution business activities include business development services and community empowerment, either through loans or financing in micro-scale enterprises to members and communities, management of deposits, as well as providing business development consulting services. Business activities that may be made conventionally or under *Syari'a* Principles. Micro financial institution may engage in fee-based activities as long as they do not conflict with legislation in the financial services sector. Legal Entity of micro finance institution are Cooperative (*Koperasi*) or Limited Liability Company (at least 60 percent owned by local government of regency/municipality or village-owned enterprise entity, the remaining share ownership of company may be owned by Indonesian citizen or cooperative with ownership of Indonesian citizen at most 20%) (ojk.go.id, 2016).

Baskara (2013) stated the scope of the business area of a micro finance institution is located within one village/sub-district, or district/municipality area according to the business scale of each. Martowijoyo (2007) also defined business scale of micro finance institution is defined based on the borrower's or Financing customer's distribution as follows:

(1) Have a business scale of village if they provide loans or financing to the population in 1 (one) village with amount capital consist of Rp. 50, 000,000.

(2) Have the scale of the district business if they provide loans or financing to the population in 2 (two) villages or sub-district or more in one same sub district with capital consist of Rp.100, 000,000.

(3) have district or city business scale if they provide loans or financing to residents in 2 (two) sub-districts or more within 1 (one) same district/city area, with amount capital consist Rp.500, 000,000.

According Financial Services Authority since 2016 micro finance institution can transform is compulsory to adjust the articles of association, incorporated, minimum capital requirements, comply with the provisions of directors and board of commissioners. And have adequate infrastructure and human resources. Financial Services Authority determines the coverage of a single district area.

The Role of Microfinance Institutions for the Sustainability of Micro Entrepreneurs:

Article 1of Law Number 20 Year 2008 mentioned that: First, micro business is productive enterprises owned by individuals and usiness entities that meet the criteria micro entrepreneur as stipulated in law invite. The law states that Micro entrepreneur is a productive enterprise owned by a person or an individual and / or a private business entity having criteria as follows: have a of at most Rp.50.000.000,00 (five tens of millions of rupiah) excluding land and building of business premises, or owning annual sales result at most Rp.300.000.000,00 (three hundred million rupiah). Micro entrepreneur may be characterized as follows: (1)The type of business goods is not always the same, at any time may change; (2)The place of business is not always permanent, at any time may move place; (3)There is no financial administration even simple, sometimes not separating family finances from business finances; (4)Business actors do not have adequate entrepreneurial spirit; (5)Low average education level; (6)Generally not access to banks, but some have access to non-bank financial institutions; (7)Generally do not have a business license or legality requirements including Tax Identification Number. While the Central Bureau of Statistics categorize itself based on the number of its workforce of micro business has only one to the workers. With the above characteristics micro businesses are more accessible to microfinance institutions in maintaining their business than formal banking institution (Kara, 2013).

In fact, the micro finance institution function is no different from the institution formal banking. But because several factors, such as complexity of the administration, micro business actors prefer micro financial institutions to solve funding problems (Kara, 2013; Hidayati, 2014). In terms of as a financial intermediary institution, which in it also assumes the trust of its customers or members placing the funds (Saleh and Hidayat, 2011). In accordance with sound credit principles, the credit provided by microfinance institutions has a very different essence from commercial credit, ie that microcredit must be part of a long-term fund-raising process called capital, for the borrower. This principle is absolutely the foundation of the loan policy that should be developed by every microfinance institution. While the ability of long-term capital formation is stubborn on one's ability to manage loan funds for productive enterprises, so the result is not only able to return principal and interest and other costs, but the borrower has a surplus that will increase the capital or funds he already has.

Although in general the cost of funds loans from micro finance institutions are slightly higher than bank interest rates, but in the side procedures loan administration. Micro finance institutions especially for non-bank have some advantages. Among the advantages such as there is no requirement such collateral is applied on formal banking. Even inside some types of micro finance institutions more loans based on trust as usual the borrower is already known by the manager. Another convenience is liquefaction and a very lucrative loan repayment flexible and often tailored to cash flow borrowers (Susila, 2007). It can be explain that on institutions formal finance is generally a treat small business is the same as business medium and large in submission financing, among which include sufficiency guarantee, capital, or feasibility business (Pelegrina, 2008). Without adequate access to micro finance institutions, almost all poor households will rely on their own limited financing capabilities or on informal financial institutions such as loan sharks, middlemen or moneylenders. This will limit the ability of the poor to participate and benefit from development opportunities. The poor should instead be empowered so they can get out of the poverty cycle (Kara, 2013).

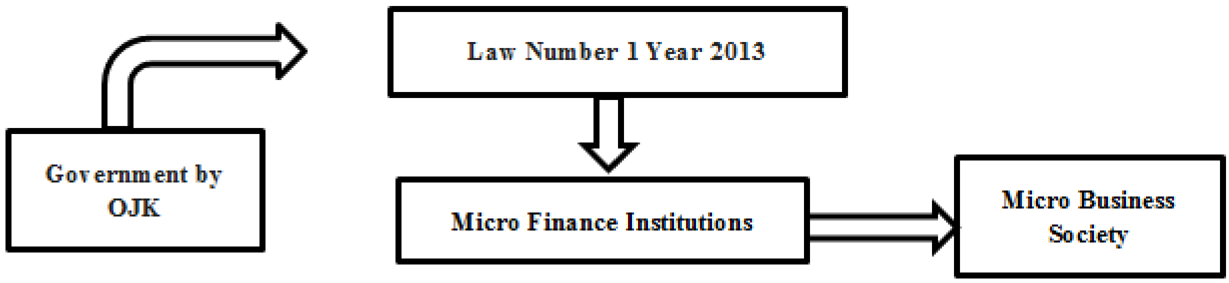

Fig 2: Practices Roles of Micro Finance Institutions in Indonesia

There are several challenges in the operational implementation of micro finance institutions: (1) Credit challenge refers to not paid by the customer for their loan. Including some problems such as loans are often granted without guarantees, or using non-traditional collateral, if loans are mostly to the agricultural sector, limited geographical distribution (e.g. loans to only a few districts), which may increase the risk of portfolios for the microfinance institutions concerned. (2)Market challenge that refers to the loss due to changes in the cost of funds in the market and the costs of investments made by microfinance institutions. To overcome this microfinance institutions should have a competitive advantage not only provide financial assistance but also provide assistance and even training for micro business actors. (3)Human resource management (generally because management is too dependent on some individuals and fraud) is also considered a component of operational challenges. To overcome it must have a human resources structure that leads to the skills of knowledge ability of good management and care about micro business management. Finally, regulation and compliance challenge that show institution should obey to regulation. Based on applicable law microfinance institutions made formal.

Conceptual Framework:

This paper aims to develop a conceptual framework on the relationship of the role of microfinance to the sustainability of micro entrepreneurs. Specifically, the literature review shows that the roles of micro finance institutions such as financial services and non-financial services will support the sustainability of micro entrepreneurship through internal factors of those micro entrepreneurs such as motivation and attitude. The sustainability of the micro entrepreneurs will represent in their intention to sustain their business (Figure 3).

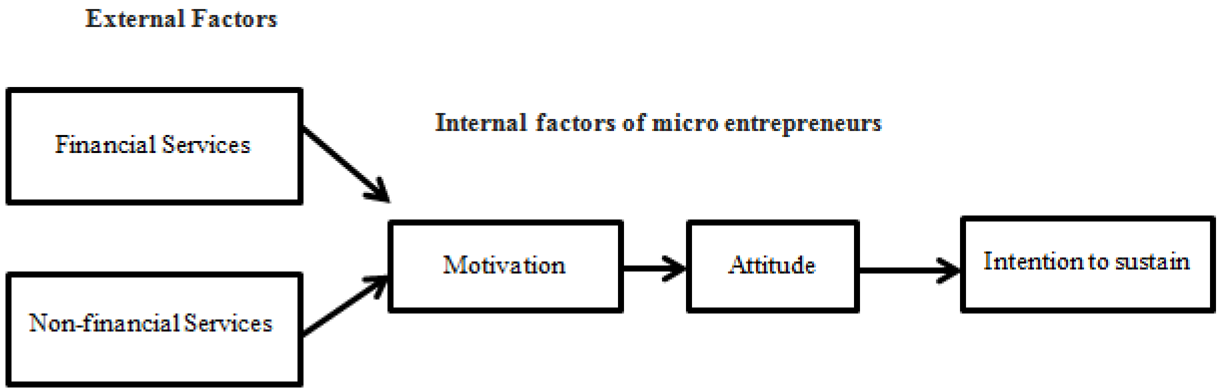

Fig 3: A Conceptual Framework

III. CONCLUSION

Efforts to eradicate poverty in Indonesia can be done by providing opportunities for micro business actors to develop. In fact, micro and small businesses are very limited. Limited in the field of capital, limited in technology, marketing, network, human resources, and so forth. So the micro finance institution is one of the media that can help in terms of capital. The good impact is Indonesia's economic development currently followed by the number of micro finance institutions that are growing very rapidly. Micro finance institutions are given the legal umbrella of the Act so that their activities are legal because if they do not have permits according to the laws and regulations are considered illegal. Most micro finance institutions do not yet have legal entity status. This is because its size is mostly small or limited board so it is difficult to meet banking and cooperative requirements. Therefore, in order to encourage the development of micro finance institutions, government raise Law Number 1 Year 2013 on Microfinance Institutions. The operational implementation of micro finance institutions controlled by the financial services authority as an extension of the government.

The importance, micro finance institution is not only to seek profit, but also to increase the income and welfare of the people and to help increase the economic empowerment and productivity of society. Micro business actors tend to choose micro finance institution as solution for funding because systems and procedures are easier than existing banks. Consider into the challenges, micro finance institution role is still indispensable on the basis of the benefits. Micro finance institutions should take role not only in facilitating the provision of capital funds, but also for the development of micro business. The role of micro finance institutions that are supported by easy access, procedures and proximity to the community will help the empowerment of the poor especially to increase their productivity through small businesses. Then micro businesses are not to be continuously dependent on the ability of others or themselves which are very limited and can improve their standard of living. In macro perspective can help alleviate poverty in Indonesia.

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