Community-based Institutional Financing Model through Cooperatives for Micro and Small Enterprises

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A R T I C L E I N F O

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A B S T R A C T

Micro, small, and medium enterprises (MSMEs) have become the main drivers of the society's economy, but limited access to financing is still a main obstacle in the development of this sector. This research aims to assess the effectiveness of cooperatives in providing sustainable and inclusive access to finance for MSMEs. Through a literature study approach by tracing references from relevant scholarly works prior to 2012, this research highlights how cooperatives, with their membership and family principles, can bridge the inequality between the capital needs of MSMEs and the constraints posed by the formal financial system. Cooperatives are able to offer a more humane and localized approach to financing, relying on social closeness, trust among members, and internal supervision mechanisms. The effectiveness of cooperatives is strongly influenced by the quality of governance, managerial capacity, and adequate supporting policies. This research concludes that strengthening cooperatives in terms of institutions, regulations, and synergy with the national financial system is an important step to expand the scope of MSME financing in a justice manner. The results of this research are expected to be an academic and practical reference in the development of cooperatives as community-based financial institutions oriented towards society economic empowerment.

INTRODUCTION

The economic life of the society cannot be separated from the role of small and medium-scale enterprises actors that are widely spread in various regions. MSMEs are the backbone of the economy because they are able to create jobs, reduce poverty, and encourage local economic growth. One of the structural barriers often faced by MSME actors is limited access to adequate sources of financing. In the conventional financial system, strict administrative and collateral requirements are often the main barrier for small enterprises actors to obtain capital support (Lindawati, 2014).

Cooperatives have emerged as institutions rooted in the spirit of solidarity and member participation, which have great potential to bridge the financial access inequality experienced by MSMEs. Through a more inclusive and membership-based approach, cooperatives have the advantage of understanding local conditions and the real needs of micro and small enterprises actors (Anairi & Radi, 2017). Cooperatives are not only a source of funds, but also a vehicle for economic empowerment that strengthens the bargaining position of MSME actors in a competitive market.

In many countries, cooperatives have been shown to play a significant role in building justice and more sustainable alternative financial systems. The savings and lending cooperative model, for example, has evolved as a main instrument in supporting productive sector financing at the grassroots level (McKillop et al., 2020). With their flexible and member-welfare-oriented schemes, cooperatives can catalyze small enterprises growth while strengthening community-based local economic structures (Nwankwo et al., 2012).

The contribution of cooperatives to access to finance for MSMEs is still not optimal. There are large variations in the institutional capacity, governance, and quality of services offered by cooperatives in different regions (Thomas & Faruq, 2017). It is important to dig and review the various literature research that has been conducted on the effectiveness of cooperatives' role in promoting MSME financing, in order to gain a more comprehensive and evidence-based understanding.

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The main problem faced in the relationship between cooperatives and MSMEs lies in the inequality between the potential of cooperatives and the operational reality on the ground. Many cooperatives do not yet have a transparent and accountable financial management system, thus reducing trust from external parties, including MSME actors who should be their main partners. This is reinforced by Gibb's (1990) findings that highlight the importance of managerial capacity in determining the effectiveness of microfinance institutions.

Structural issues such as limited human resources and weak regulatory support also hamper the ability of cooperatives to expand financing coverage to MSMEs. According to Schumacher (1973), resilient institutional structures and supportive policies are two key elements in building sustainable financial institutions for the informal sector. Unfortunately, many cooperatives still operate within a policy framework that does not fully empower them as alternative financial institutions.

The lack of integration between cooperatives and the national financial system means that cooperatives are often isolated from the broader financing network. The lack of access to secondary sources of funding or institutional guarantees makes it difficult for cooperatives to compete with other formal financial institutions. This is highlighted by Yunus (2003) in his work on the Grameen Bank, where he emphasizes the need for synergies between community financial institutions and the national financial system to increase the financing capacity of the micro sector.

The diverse and widespread dynamics of the MSME sector require a flexible and adaptive institutional approach. Cooperatives, with their democratic and participatory values, are theoretically capable of meeting these challenges. This potential will only be realized if there is an understanding of the various forms and models of successful cooperatives and lessons learned from best practices in various geographic and social settings. The literature research is an important instrument to summarize existing knowledge and strengthen future policy directions and institutional practices.

In the midst of inclusive economic development efforts, cooperatives have a strategic position that cannot be ignored. Their role is not only as a financing provider, but also as a local economic development partner capable of fostering and assisting small enterprises actors in the long term (McKillop et al., 2020). Given the large population of MSME actors and their impact on the socioeconomic structure, a deeper understanding of the relationship between cooperatives and MSMEs is crucial in formulating a more justice and sustainable development approach.

This study aims to examine the extent to which cooperatives are able to play a strategic role in expanding access to financing for MSMEs. Through a literature study approach, this research will review academic and empirical findings related to the effectiveness of cooperatives in supporting the small and medium enterprise sector, both from the institutional, regulatory, and financing models that have been implemented. The results of this research are expected to make an academic contribution to the development of community-based economic institutional theory, provide a basis for consideration for policy makers and cooperative actors in increasing their financial intermediation function.

RESEARCH METHOD

This research uses a qualitative approach with the literature study method as the main basis for data collection and analysis. The literature study was chosen to examine various results of previous research, both in the form of books, scientific journals, research reports, and relevant policy documents, in order to understand the contribution of cooperatives in increasing access to financing for MSMEs. According to Moleong (2007), a qualitative approach aims to understand social reality in depth through the collection of information derived from various valid and verifiable secondary sources. The approach allows researchers to identify patterns, trends, and thematic relationships between the existence of cooperatives and their ability to provide inclusive financing for the MSME sector. The literature reviewed included references from national and international institutions that focus on community-based economic development and strengthening microfinance institutions.

The analysis technique used is content analysis, which aims to interpret the meaning of text within a certain scope systematically and objectively. Content analysis is very effective in literature studies because it allows researchers to organize categories, themes, and theoretical constructions from extensive reading (Krippendorff, 2004). All secondary data were thematically reviewed based on the key variables of cooperatives, financing, and MSMEs. The data were then compared and critiqued to build a comprehensive framework for understanding the extent to which the role of cooperatives has been empirically recognized in increasing financial accessibility for micro and small enterprises actors. The steps implemented follow the systematic procedure advocated by Neuman (2006), namely source identification, literature selection, data recording, content classification, and interpretative inference. Thus, this method not only provides a descriptive overview, but is also able to present a comprehensive conceptual synthesis.

RESULT AND DISCUSSION

Increasing access to finance for MSMEs has been a challenge that many countries continue to struggle with, especially in developing countries. MSMEs play a vital role in the economy, but they often face significant barriers in gaining access to adequate sources of financing (Nyikos, 2015). Amidst these limitations, cooperatives have emerged as a promising alternative. With their member-based organizational structure and principles of solidarity, cooperatives are able to offer more adaptive and community-based financing, which better understands the local characteristics and needs of micro and small enterprises actors (Nwankwo et al., 2012).

Cooperatives differ from commercial financial institutions in general, which tend to emphasize efficiency and profitability (Poderys, 2015). As economic institutions based on collectivity and democracy, cooperatives provide their members with the opportunity to not only obtain financing, but also to actively participate in decision-making. This creates a more personalized relationship between the cooperative and its members, and allows for more flexible financing that is based on real needs. With this model, cooperatives are expected to be the bridge that connects MSME actors with the resources they need to develop.

In recent years, attention to cooperatives as providers of inclusive financing is strengthening. Policymakers and academics recognize the great potential that cooperatives have in creating a more equitable and justice economic system. In developing countries, where most MSMEs are still marginalized from the formal financial system, cooperatives are the entities that are able to fill the void. They not only help in the provision of capital, but also play a strategic role in local economic empowerment and reducing social inequality. It is important to dig deeper into how cooperatives can continue to develop and expand their financing outreach to MSME actors in the future (Imarhiagbe, 2016).

Efforts to increase access to finance for MSMEs demand attention to financial institutions that are more adaptive and accommodating to the conditions of enterprises actors in this sector. Cooperatives, as member-based economic entities, offer a different approach than commercial financial institutions. The more collective and democratic approach of cooperatives makes them closer to the socioeconomic realities of the lower society (McKillop et al., 2020). It is within this framework that cooperatives have the potential to provide more friendly, flexible, and sustainable access to financing for MSME actors. As awareness of the importance of an inclusive economy grows, so does attention to the role of cooperatives among policymakers and academics. The role of cooperatives in supporting the informal sector is crucial, especially in developing countries with unequal economic structures.

To be able to provide inclusive financing, cooperatives must have an understanding of the characteristics and needs of MSMEs. This includes aspects such as production capacity, enterprise risk, and income cycle. The advantage of cooperatives lies in their ability to establish a close relationship with their members, so that they can design financing schemes that suit real conditions. In the classic literature on cooperatives, Hanel (1989) emphasized the importance of contextual understanding in designing cooperative services that are relevant to the needs of its members. This approach differs from the one-size-fits-all approach often used by commercial financial institutions. Through accurate needs mapping, cooperatives can create financial services that are truly useful and powerful.

It is also important to pay attention to the organizational structure and governance of cooperatives in providing sustainable financing. Cooperatives that are managed with the principles of transparency, accountability, and active participation of members have better resilience in carrying out financial intermediation functions. According to Braverman and Guasch (1986), good governance is a main requirement for microfinance institutions to survive and develop in the long term. Weaknesses in management are often at the root of cooperatives' ineffectiveness in meeting the financing needs of their members. Strengthening managerial capacity and internal supervision systems are important aspects in strengthening the role of cooperatives.

Empowering cooperative members is also key in creating an inclusive financing system. Cooperative members not only act as beneficiaries, but also as owners and managers of the institution itself. This makes active member participation the cornerstone of cooperative success. Financial literacy becomes an important instrument to ensure that members understand their rights and obligations in the cooperative. This empowerment creates a sense of belonging and shared responsibility, which in turn promotes the sustainability of cooperative operations and strengthens social ties among members. As stated by Seibel (1990), member education is a crucial element in creating resilient cooperatives that can withstand market pressures. This education includes an understanding of financial products, lending repayment mechanisms, and participatory roles in decision-making.

Expanding access to finance through cooperatives also relies heavily on institutional network support. Cooperatives cannot stand alone in the financial ecosystem; they need access to secondary funding sources, partnerships with guarantor institutions, and integration with the national financial system. The absence of this support will limit the space for cooperatives to massively channel financing to MSMEs. According to Adams, Graham, and Von Pischke (1984), the success of microfinance institutions, including cooperatives, is largely determined by the extent to which they can build productive institutional linkages with other actors in the financial system. This integration allows cooperatives to access the liquidity needed to expand their services.

In carrying out their functions, cooperatives also need to pay attention to innovation in financing services. Information technology can be an effective tool to increase operational efficiency and expand the reach of cooperative services, especially in remote areas. Digitalizing administrative processes, recording transactions, and financial reporting will help cooperatives operate more professionally. As stated by Christen, Rhyne, and Vogel (1995), technology adoption in microfinance institutions should be tailored to the capacity of the organization and the readiness of human resources. Technological innovations must be accompanied by adequate training in order to be implemented effectively.

Cooperatives that want to provide inclusive financing must also be inclusive of vulnerable groups in their communities. Many MSME actors are women, people with disabilities, or indigenous society, who are often excluded from conventional financial services. Cooperatives can be an effective channel to reach out to these groups, provided that the principle of inclusivity is truly implemented in their institutional practices. Cooperatives have great potential in supporting the empowerment of marginalized groups if supported by policies that are sensitive to social diversity.

The sustainability of cooperative financing is not only about the availability of funds, but also includes aspects of social and institutional sustainability. This means that cooperatives must be able to maintain member trust, build solid governance, and continue to adapt to the dynamics of the external environment. Meyer and Cuevas (1992) state that the success of microfinance institutions depends largely on the balance between financial sustainability and social mission. In cooperatives, this balance can be achieved through prudent risk management and the establishment of justice but firm lending policies.

As financing providers, cooperatives must also embed the principle of social responsibility in all their activities. This means that cooperatives not only extend credit, but also foster, assist, and ensure that the financing is used productively. This social responsibility is a main differentiator between cooperatives and profit-oriented financial institutions. According to Huppi and Feder (1990), successful community-based financial institutions are those that are able to create long-term relationships and build economic solidarity among their members. This approach strengthens the cooperative's resilience in uncertain economic situations.

Cooperative financing schemes should be designed with the diverse needs of MSMEs in mind. Each enterprise actors have different characteristics and needs; for example, some require short-term working capital for day-to-day operations, while others may need long-term investments for enterprises development (Oladejo, 2013). An effective cooperative is one that is able to identify and understand the specific needs of its members, and develop a varied portfolio of financing products (Begajo, 2018). In this way, cooperatives can provide appropriate and relevant solutions to their members, thereby increasing their chances of enterprises success.

Differentiation of financing products is an important strategy in strengthening the relevance and effectiveness of microfinance institutions, as expressed by Von Pischke (1991). By offering different types of products, ranging from working capital lending, investment financing, to training and mentoring programs, cooperatives can reach more enterprise actors and meet their needs more comprehensively. This not only helps cooperative members access appropriate financing, but also promotes local economic growth and improves the competitiveness of MSMEs. As such, cooperatives that are responsive to the needs of their members will be better able to contribute to inclusive and sustainable economic development (Cuomo, 2015).

The active engagement of government and policymakers greatly influences the effectiveness of cooperatives in providing financing. Supportive regulations, fiscal incentives, and training programs can encourage the growth of healthy and professional cooperatives. In this case, a policy approach that recognizes the unique characteristics of cooperatives is needed. As Birchall (2003) explains, public policy should avoid a top-down approach and instead facilitate the participation of cooperatives in the formulation of local economic development strategies.

Cooperatives also need to establish an internal evaluation system to measure their financing performance. This evaluation should not only be based on lending repayment rates, but also on the social and economic impact on the lives of their members (McKillop et al., 2020). With a comprehensive monitoring system in place, cooperatives can continuously improve their policies and be responsive to the dynamic needs of the field. This evaluation is also important in maintaining the cooperative's transparency and accountability to all stakeholders, including members and external partners. According to Ledgerwood (1999), monitoring and evaluation is an integral part of effective and accountable microfinance governance. By implementing regular, data-driven evaluations, cooperatives can make adaptive adjustments to the socio-economic dynamics in their communities. This supports the creation of cooperatives that are responsive, competitive, and truly fulfill their function as institutions that champion the welfare of members.

From all these descriptions, it appears that cooperatives can effectively provide sustainable and inclusive financing if they are able to strengthen their institutional capacity, expand their networks, adopt appropriate innovations, and implement participatory governance. The role of cooperatives should not be seen as an alternative, but rather as the main actor in realizing a justice and community well-being-oriented financial system. The development of strong and resilient cooperatives is a strategic step in answering the challenges of MSME financing that have not been fully resolved so far. Cooperatives have the potential to be the main driver of an inclusive people's economy with its characteristics based on solidarity and shared ownership.

CONCLUSION

Cooperatives have a significant capacity to become a main pillar in expanding access to finance for MSME actors. Through the principles of membership, togetherness, and member well-being-oriented services, cooperatives are able to overcome various barriers that often prevent MSMEs from accessing conventional financing. The success of cooperatives in providing sustainable and inclusive financing is highly dependent on their institutional quality, management professionalism, and favorable regulatory support. The results of the literature study show that cooperatives with good governance systems, transparency, and close relationships with local communities have proven to be more effective in channeling productive financing to the MSME sector in a justice and sustainable manner.

From the results of this research, it is clear that strengthening cooperatives as community-based financial institutions not only has an impact on increasing access to financing, but also on strengthening the overall economic structure of the society. Cooperative empowerment has a close correlation with increasing the capacity of small and micro enterprises in creating economic added value and resilience to market fluctuations. The cooperative institution should be seriously included in the national economic development policy framework that is inclusive and society-based. The implications also touch on the need for policy reforms that support the cooperative ecosystem through human resource training, digitization of services, and strategic partnerships between cooperatives and the formal sector.

It is recommended that the government, financial institutions, and academics work together to design a cooperative institutional model that is resilient and adaptive to the needs of MSMEs in various sectors. Increasing management quality, cooperative financing product innovation, and access to digital technology should be prioritized in the cooperative renewal agenda. Further research needs to focus on leading cooperative practices that have successfully reached a wide range of MSMEs, to then serve as a reference in the development of cooperatives nationwide. The principles of good governance, transparency, and accountability must also be upheld as the foundation of trust and sustainability of cooperatives in supporting the financing of the small and medium enterprise sector.

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