

## **The Factors Influence the Success of Small and Medium Enterprises: Case Study in Batu City, Indonesia**

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**Abstract:** A study was carried out to understand the factors influence the success of Small and Medium Enterprises (SMEs) in Batu City. This report was based on the secondary data collected from the Office of Cooperative Industry and Trade Batu, city and primary data obtained from the SMEs actors. The secondary data collected include the numbers SMEs, types and kind of business and the development of SMEs. The primary data collected the background of the owner, management system, the way they managed the SMEs, threats of their business. The result show that most of SMEs in Batu City (67%) have their business in Agro-industry. This is in accordance with its mission as the “Agropolitan City”. Batu City also declares as the tourism city with its branding “Kota Wisata Batu (KWB)”. This branding support the development of SMEs in Batu city. The success of enterprises was influenced by the characters and behavior of the owner. The success entrepreneur was more creative, especially in gaining the capital, increasing their knowledge and skills and marketing. The fail or non-success enterprises because the owner is passive in obtaining information and marketing channel.

**Key words:** Small business, entrepreneurs, cooperative, SMEs, management system, factors influence

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### **INTRODUCTION**

Small and Medium Enterprises (SMEs) has been considered as a source of employment and economic income in many developing countries (Mead and Liedholm, 1998). Sri Mulyani, the Minister of Finance, state that SMEs is the backbone of Indonesian economic. This statement is in accordance with the fact discussed by BICG (2015) which stated that the Indonesia economy is basically characterized by grassroots SMEs. The SMEs in Indonesia made up more than 99% of the total enterprises numbers. In term of enterprises numbers, the small and medium entrepreneurs account for about 41 million units whereas the medium size enterprises is about 60,000 units and the larger entrepreneurs is only about 20,000 units. In 2000, SMEs accounted for 89% of total employment.

According to the Law No. 9 of 1995 small enterprises are defined as the enterprises owned by Indonesian citizens; independent and are not affiliated with large enterprises. These are individual businesses with or without legal licensing. Although, does not owned by individual, cooperative is also classified as the small enterprises. Therefore, the ministry look after these enterprises is called the Ministry of Cooperative and Small and Medium Enterprises. Looking from point view of

assets and sales volume the small enterprises are the enterprises with assets of <Rp. 20 million (excluding land and building) and annual sales volume of not more than Rp.1 billion. The medium enterprises are the enterprises with assets of more than Rp. 20 million (excluding land and building) but <Rp. 10 billion (US\$ 1.176 million) and with sales annual of more than Rp. 1 billion.

A lot of SMEs are deal with agricultural sectors, especially, those who related to food and drink industries (Muljani and Nagel, 2012). Although, the contribution of agriculture to employment and country income decreases as economic grows but the importance of agriculture in the developing countries is still very important (Fatah, 2007). However, it is the time that agriculture is not only considered as a passive sector, it should be viewed from the context of transformation process. Hence, agriculture should be linkage to industry, because agro industry has strong linkage with other sectors. The linkage is not only its product but also with final demand and primary inputs. These are the relationship with consumption, investment and labor.

The role of SMEs in Indonesian economy has been widely recognized. However, the development of SMEs did not always encouraging. In the year of 1997, for example, the Indonesian Bureau of Statistic showed that,

there was 39, 765, 110 units of SMEs in Indonesia, these numbers decreased to only 36, 813578 units in 1998 and again increased to 41, 362, 315 units in 2002 (BPS, 2003). These manuscript discussed the factors influenced the success of small and medium enterprises. The discussion was based on the data obtained from agro-industry SMEs in Batu city, Malang, Indonesia.

### **Literature review**

**SMEs condition in Indonesia:** Most of SMEs in Indonesia are based on traditional industry; owned and managed by the management with low education level of education. Wicaksono (2013) cited the data of Asia Foundation which showed that more than 79.3% of entrepreneurs who managed SMEs in Indonesia was graduated from senior high school and/or a lower level. From these numbers, 16.7% graduated from elementary school and even 4.4% did not have any formal education background, they are probably not able to write and read.

This low educational background of SME's owners has made very difficult for SME's to create many innovations in their product. It also face a gap in terms of technology and training. In other side, globalization has made a very strong international competition, especially for the product quality. Most of SMEs owner or manager did not know about National Standard Certificate, International Standard Organization (ISO), Standard Operational Procedure (SOP) or about intellectual properties. Only about 47.8% of MSME's owners have registered their company while the rest do not have permit at all. They know that there is a chance to export their product but they did not know how to export their product to overseas. In addition, since the production is based on the traditional industry, it is very difficult for mass production. Therefore, the SMEs difficult to meet demand in a large numbers.

Capital is considered as one of the key factor that made SMEs in Indonesia difficult to grow, even only to maintain their activities. Limited access to finance has been known as the barriers to SME. Small business often faced lack sufficient collateral for loans. Indonesian government has overcome this problem by program what they called "Kredit Usaha Rakyat (KUR) or credit for people business scheme". This scheme is aimed at nurturing small business growth. The Ministry of Finance provides insurance for 70% of loans given to SMEs with banks taking on the remaining 30% of the risk. In 2014, there was the six participating national banks provided more than 11.3 m SMEs with a combined Rp. 146.3 trn (\$11.2 bln.) of funding under the KUR program.

Most of Indonesia MSE possess a limitation in marketing access. In the information technology century,

online marketing is very important. However, due to low education background only a few Indonesian SMEs have an access to internet connection. Report by DC (2015) showed three quarters of Indonesia's SMEs are missing out on most of the benefits of digital technologies; over one-third of Indonesian SMEs are offline while another 37% have only basic online capabilities such as a computer or broadband access and only 18% have what the report defines as intermediate engagement (use of websites and social media) and only 9% have advanced engagement with e-Commerce capabilities. To overcome these problems, the report outlines key directions for government policy to support digital local SMEs including: increasing broadband access; helping all SMEs to be digital businesses, expanding e-Payments; expanding access to finance and expanding e-Government services.

Increasing broadband access was considered very important because the existing internet access in Indonesia is relatively expensive and slow. Therefore, increasing broadband access and the quality of service will encourage digital technology adoption by SMEs and could improve the performance of existing technologies. Expanding e-Payment would improve the trust in e-Commerce payment platforms. This will increase bankability of Indonesian consumers and businesses and it is expected that alternative payment systems will increase the volume of digital transactions. Digital SMEs could provide an information, both domestic and international sources of finance, hence it would expand the access to finance. Expanding e-Government services is necessary because government could deliver through online platforms and these will make more cost effective and efficient. More online government services would build consumer confidence in online activities and services over time.

According to Wicaksono (2013), bureaucracy is one of the important issue to initiate business in Indonesia, especially for Medium, Small and Micro Enterprises (MSMEs). There are a lot of regulation in which many of them are overlapped. There are a conflicting regulation between central government and province or district. It is not as easy to get license for opening enterprise, it will take a complex process and a long time.

Realizing the importance of SMEs in 1993 Indonesian Government established the Ministry of Cooperatives and Small and Medium Enterprises. Then, in 1995 the Law No. 9 of 1995 for small enterprises was enacted. The main objective of this law is: to create a conducive business environment and to strengthen the capacity and capability of the SMEs as the important economic actors.

For implementing these objectives, there was 6 main programs had been formulated which is called “the six action plans”. This plan was aimed at promoting SMEs. These are:

**Creating a business-conductive environment:** The government will make easier regulations required by SMEs establishment and development.

**Market access:** The government works for facilitating market access and opportunities.

**Financial access:** The role of the government is divided into two areas. The government can provide a special scheme for SMEs, setting up regulation for making easier the SMEs to get loans from bank and cooperate with financial institutions to provide financial resources for SMEs.

**Information access:** This program is a part of marketing access plan, a current weak point in SME marketing. The action of government is to help the SMEs with business networking through information technology.

**Technology access:** This action is intending to promote technology and technology sharing for SMEs. The government will assist the SMEs in the field of increasing awareness to apply proper technology to the enhancement of competitiveness both in term of productivity and quality.

**Human resources development:** As discussed before, one of the weakness of SMEs in Indonesia is a low background of owners and management. Therefore, government will improve organization and management capacity of the SMEs.

**Factors influence the success of entrepreneurs:** The success of the SMEs is mostly depend on the entrepreneur characteristics and behavior. The list presented here was based on the review of some research and analysis of many professionals and institutions. These are some critical and important factors that will determine an entrepreneur to be a successful entrepreneur. First, entrepreneurs should poses the characters of willingness to take an action. Actions make the idea can be exist in real world. Without doing action, no business and hence there will no a successful business owners. The following list is the other factors which should be taken in account by an entrepreneurs.

**Creativity:** Entrepreneurs must be creative person. The creativity will determine the success of the business.

Entrepreneurs must creative in all aspects of business, starting from determine the type of business and product, creative increasing knowledge and skill, creative in finding the capital to creative in creating marketing.

**Patience and persistence:** Entrepreneur must be patient and ready to continue even if you lose the first battle because the war is still not finished. It's only the beginning of your journey as an entrepreneur. Entrepreneurs should be persistence that is do not given up from threads, even though this threat could make your business fail.

**Risk tolerance:** There is no guarantee that once you work, you will success. Therefore, entrepreneurs should persons who are willing to take a risk. However, in order minimize the risk he should able to calculate the risk.

**Self-confidence:** Self-confidence is important and key factor for entrepreneurs to be success. Self-confidence will make entrepreneurs having risk tolerance characters. Self-confidence will make they dared to start doing and managing their own business.

**Knowledge, skills and experience:** Knowledge, skill and experience is very important factors that will determine the success of entrepreneurs. However, you do not need afraid to start your business even though you do not have knowledge, skills and experience. They can be learned while you run your business. Therefore, creativity as discussed in the first list is one of the most important factor determining the success of entrepreneurs.

**Great talent:** Talent is believed inborn in an entrepreneur. However, sometimes talent is something that can be replaced with knowledge and skills. Therefore, you should have enough knowledge and skills to be a successful entrepreneur.

**Connections:** Network is very important in business. More connection means more possibilities for building a successful business.

## **MATERIALS AND METHODS**

The study was carried out in Batu city, East Java, Indonesia. Batu City was chosen because the city has ben declared as “Agropolitan city” with its branding “Kota Wisata Batu (Batu Tourism city), KWB”. The development of SMEs in this city is very fast.

The data collected was the secondary and primary data. The secondary data collected include the numbers SMEs, types and kind of business and the development

of SMEs. The data was collected from the Office of Cooperative Industry and Trade (Dinas Koperasi, Industri dan Perdagangan) Batu City.

The primary data collected by open interview with the selected SMEs. The selection of SMEs was based on the success and failure of the SMEs. The SMEs was considered as the success SMEs if the business develop and sustain and the fail SMEs if they could not sustain their business. The data of the success and fail SMEs was obtained from the Office of Cooperative Industry and Trade, Batu City. The 10 success SMEs and 10 fail (non-success) SMEs were interviewed. The data collected include: the background of the owner, management system, the way they managed the SMEs, threats.

## RESULTS AND DISCUSSION

**SMEs condition in Batu City:** Since, it was declared as the “City District”, the economic growth of Batu City is always higher compared to the national economic growth. In the year 2012, for example, economic growth of Batu city was 8.25% whereas in the national economic growth was only about 6.2%. This condition occur also in 2016 in which the economic growth Batu city was 8.03% compared to the national economic growth of 5.04%. The role of SMEs in economic growth and reduce unemployment of Batu city is very significant. According to the Head of Office Cooperative Industry and Trade Batu city, the role of SMEs increased from year to year in 2013 for example, the SMEs contributed about 42% of original city income, increased to 59.8% in 2016 and employed about 87% of work force.

In respect of the importance of SMEs for economic of Batu City, the government of Batu city targeted the growth of SMEs by 300 units/year. Until 2014, this target could be achieved, even exceeded (Table 1). In 2014 the target was lowered to 150/years. Nevertheless, it turns out that the target could not be achieved. Apparently, there was already too much SMEs number. Hence, although, there was establishment of new SMEs, the existing SMEs could not further maintain their business (Table 2).

The SMEs in Batu city are dominated by agriculture business (about 66%) and then followed by services (12%), processing (7%). The high number of SMEs doing business in agriculture is in accordance with the declaration Batu City as the “Agropolitan city”. The types of business are flower nursery, food processing such as chips, crackers and fruit juice. Batu is famous with its potato and apple chips and apple juice.

Batu is also famous as tourism city with its branding “Kota Wisata Batu (Batu Tourism City), KWB”. This

Table 1: Development of SMEs in Batu City, form 2008-2016

Years	No. of SMES
2008	8.300
2009	11.000
2010	11.862
2013	14.570
2016	14.649

Table 2: Business type of SMEs in Batu City

Type of business	No. of SMES
Agriculture	9.689
Food processing	1.047
Hotel and restaurant	921.000
Transportation	1,004.000
Services	1,788.000
Others	190.000

Office of Cooperative Industry and Trade, Batu City

branding has very significant effect on the development of SMEs in Batu City. The SME is mostly doing their business in the field of food processing and restaurant. In addition, lately in Batu develop “wisata petik buah (fruit picking tourism); wisata petik sayur (vegetable picking tourism) and wisata petik bunga (flower picking tourism). By this type of business, tourist can pick fruit (especially, apple, orange and strawberry), vegetable or flowers directly from the farmer’s farm.

To support the Tourism, government encourage the establishment of hotel and restaurant and services (Table 2). There are 4 hotels with 4 stars categories and 6 hotels with 2 stars category. The services business in Batu is mostly related with travels.

The importance of SMEs for economic development in Batu has been realized (Hapsari *et al.*, 2014) but the supervisor of SMEs is only under a level of “Section” which called the cooperative, small and medium enterprises study. This study is under the Cooperative Industry and Trade Office. In other district, the institution responsible to supervise SEMs is usually at the level of “office” which usually called as the Office of Cooperative, Small and Medium Enterprises. Although, only in a level of “section”, her activity is very high. Some of the task of this study are:

- Formalizing plan action
- To prepare technical policy for SMEs nurturing and development
- To prepare the materials and curriculum for training of human resources of SMEs
- To prepare materials for organization, management and accounting development of SMEs
- To coordinate the activities of all office responsible for SMEs nurturing and development
- Monitoring, evaluation and controlling SMEs

To make easier and shorten the time of the establishment of new SMEs in 2012 the city major established an office called “Kantor Pelayanan Perizinan Terpadu (the Office of Centralized Licensing Services), KPPT”. The establishment of this office (KPPT) 1 year in the front of the establishment of the “Pusat Layanan Usaha Terpadu, Center for Centralized Business Services (PLUT)” under the coordination of the Ministry of Cooperative, Small and Medium Enterprises”.

**The factors influence the success and failure of SMEs in Batu city:** The 6 from 10 of the owner of success SMEs were had background of senior high school and the rest were graduated from junior high school. The owner of the un-success SMEs were mostly (90%) graduated from junior high school.

Both the success and un-success SMEs in Batu city started their business with their own capital (Table 3). However, most of these SMEs faced difficulty in capital for developing their business. To overcome this problem, the success SMEs have more capital resources; this include from the formal bank. Although, Indonesian government develop a credit scheme for SMEs which is called “Kredit Usaha Rakyat, Credit for people business, KUR”, only 10% of the un-success SMEs had experience applying credit to formal bank. Most of them obtain the credit from informal bank (they called bank titil) or from individual persons.

Bank Titil is informal monetary institution who do their business, like a formal bank by giving credit to any person who need it. The word “titil” means the collection the credit payment is done by day to day. To obtain credit from “bank titil” is very fast and easy. They do not need a survey and bank warranty. However, the interest is very high (can be as high as 50% per month), so that, a lot of the creditor fail to pay they credit.

Another critical factor faced by SMEs in Batu City is marketing (Table 4). The success SMEs use every chance to sell their product, include advertisement and person to person marketing. They very active used newspaper, radio and television as the media for advertisement. The success SMEs also create cooperation with travel bureau. By this system, travel bureau bring their client to the SMEs and the travel bureau get the fee from the SMEs. The result in Table 4 also show that some success SMEs have used internet marketing. The un-success SMEs, on the other hand, they passive or just wait the consumers to come, see and buy their product.

The success SMEs very active to gain information for developing their business. They active look for and come to the source of information; include newspaper, radio, television and internet and government office (Table 5). The un-success SMEs only used the conventional media

Table 3: The source of capital for success and non-success in Batu City

Source of capital	Type of SMEs	
	Success SMEs (%)	Un-success SMEs (%)
Private	100	100
Bank	80	10
Informal bank (Bank Titil)	20	80
Informal sources	20	80

Table 4: Marketing system of success and non-success SMEs in Batu City

Marketing	Type of SMEs	
	Success SMEs (%)	Un-success SMEs (%)
Passive	0.0	100.0
Advertisement	80.0	0.0
Cooperative with travel bureau	60.0	0.0
Internet	40.0	0.0

Table 5: Source of information of success and non-success SMEs in Batu City

Source of information	Type of SMEs	
	Success SMEs (%)	Un-success SMEs (%)
Unidentified	100	100.0
Newspaper	80	0.0
Radio	100	60.0
Television	100	80.0
Internet	60	0.0
Government office	100	20.0

Table 6: Kind of innovation the success and non-success SMEs in Batu city

Type of innovation	Type of SMEs	
	Success SMEs (%)	Un-success SMEs
Product	100	100.0
Packaging	80	0.0
Marketing	90	10.0

radio and television. Some of them (20%) come to Government Office because they got an invitation to participate a training.

The information sought by the success SMEs nearly all aspect of business development. From this information they did not doubt to develop many innovation, include product quality and product diversity, packaging and even marketing channel (Table 6). The un-success SMEs was hardly develop any innovation. They do the production and marketing process as usual. This means that they do the business as their predecessor.

## CONCLUSION

The study shows that the success of SMEs in Batu City was determined by the characters and behavior of the owner or entrepreneurs, especially creativity. If the entrepreneurs creative, they will active to solve the problems and the treads. They very creative and active to improve their knowledge and skill, improve their product quality and diversity and improve marketing access.

These facts do not necessary means that the other factors are not important. The willingness to take action

is still the most important factor; there will no success SMEs if the owner did not willing to start their business.

The courage to take risks is also the important factor that influence the success of SMEs in Batu city. Both the success and un-success SMEs have an experience of getting loss in their business. However, the way they overcome the loss was very different. The successful entrepreneurs immediately rising up to start their business. The un-successful entrepreneurs, on the other hand, mostly stop their business.

Connection, of course had an effect on the success of the SMEs. The practice of internet marketing done by the successful entrepreneurs was one of the effort to broaden the connection.

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