

The Role of Village Micro-Finance Institution Towards Rural Development

I Nengah Suarmanayasa^{1,*} Gede Putu Agus Jana Susila² I Wayan Cipta³

^{1,2,3} *Department of Management, Universitas Pendidikan Ganesha, Singaraja, Indonesia*

*Corresponding author. Email: nengah.suarmanayasa@undiksha.ac.id

ABSTRACT

The third *Nawa Cita* requires development to be started from villages and outskirts. Village as a source of progress in Indonesia still has various problems. One of the problems that is faced by the rural communities is the lack of capital access. This limitation is considered as the main cause of the development delays in villages. For this reason, village financial institutions, such as Village Micro-Finance Institutions (*Lembaga Perkreditan Desa—LPD*), are important to be optimized. This study aims to determine the role of LPD towards village development. Descriptive qualitative method was used for this study. Financial reports, articles, books, and descriptions regarding the role of LPD towards village development were used as the data. The result of this study found that LPD has a significant role towards village development in Bali Province. The role of LPD is reflected economically, socially, and religiously. In accordance with the mandate of Regional Government Regulation No. 3 year 2017, LPD is obliged to give about 20% of the profits for village development, and 5% for social funds. These funds are allocated to the village for poverty alleviation, improving the quality of education and providing business opportunities for rural communities.

Keywords: *Performance, Rural development, Village micro-finance institution*

I. INTRODUCTION

National development vision is the realization of Indonesia that is sovereign, independent, and has a teamwork personality. One of the changes way towards this vision is to be pursued through the development of Indonesia from outskirts by strengthening regions and villages within the unity state (the third *Nawa Cita* of the Government of Joko Widodo as a President and Jusuf Kalla as a Vice President). The strengthening of the village development paradigm is also in line with the mandate of UU No 6 Year 2014 concerning Villages. The village development targets that must be achieved in the next five years are reducing the number of underdeveloped villages and increasing the number of independent villages. Village development still poses considerable challenges because until this time the number of independent villages in Indonesia is only about 3.91 percent of the 74,093 villages in Indonesia.

Rural areas in third world countries are described as living areas of poor people who use agricultural land. There are two main issues for village development in Indonesia: First, most Indonesians live in rural areas. Currently, it is estimated that 60 percent of the population still lives in the village; Second, the welfare

of the population in the village is far left behind compared to the urban population, around 63 percent of the total poor live in the village [1].

The economic dualism model has become a strategic issue for village development in developing countries [2]. In the first phase, the objectives of village development were directed from community development (1950s) to the growth of small farms (1960s). Second, the growth of small farms was continued, integrated with village development efforts (1960s), including through technology transfer policies, mechanization, and agricultural extension. Third, there was shift in state-designed of village development (1970s) towards market liberalization (1980s) through structural adjustment policies and free markets. Fourth, village development was directed at strengthening the process approach, participation, empowerment and actors (1980s and 1990s). Fifth, the importance of sustainable livelihoods as an integrated framework in village development (1990s), including through strengthening micro credit in development. Sixth, placing village development as a strategy to reduce poverty (2000s).

The strategy to develop villages is inseparable from efforts to overcome the basic problems experienced by rural communities including poverty, lack of human resource potential due to urbanization and lack of accessibility [3]. Limitation in access to capital (credit) is one of the factors causing poverty [4]. A household survey conducted by the World Bank (2011) shows that in terms of access to loan (credit), 40 percent of people cannot borrow, 17 percent of financial are from banks and 36 percent borrow from informal financial institutions. This means that 76 percent of Indonesians cannot access formal financial institutions.

Many parties believe that microfinance and kind like that can be a tool for realizing development in rural areas. One of the custom-based financial institutions that has grown and developed in Bali Province is the Village Micro-Finance Institution (Lembaga Perkreditan Desa, LPD). LPD was established in order to improve the welfare of rural communities by creating and providing services in the financial sector. LPD is one of Balinese local wisdom that is managed from, by and for the communities (krama adat). LPD is a village-owned financial enterprise that carries out business activities in the village environment and for krama adat.

2. LITERATURE REVIEW

2.1. Endogenous Development Theory

The bottom-up rural development paradigm is known as the endogenous rural development approach. Economists introduce this approach to create a community-based economic growth model which is expected to be able to maintain and accelerate the development of local resources and industries. Revealed the basic characteristics of endogenous development for rural areas as follows:

- 1) The main principle, the special resources of a region (natural, human, and cultural) are the key to sustainable development.
- 2) Dynamic forces, local initiatives and local companies.
- 3) The function of rural areas, the economy with a variety of services.
- 4) The main problem of rural development is the limited capacity of an area and social groups to participate in economic and development activities.
- 5) Focus on rural development, capacity building (skills, institutions and infrastructure) and reduce the problem of social isolation.

Reference [5] argues that endogenous development strategies seek the satisfaction of local needs and demands through the active participation of local

communities in the development process. This development strategy is aimed not only to improve the production side (agriculture, industry and services), but also to promote social and cultural dimensions that affect people's lives. Reference [5] also emphasizes that endogenous development is related to the process of capital accumulation in a certain area (specific localities) by concerning the regional capacity in spreading innovation throughout the local production system and the role played by the local innovation system. The efficiency of using local potential is also very determined by how the institutions work in rural areas.

Reference [5] statement is also in line with the statement of Douglas C. North, an institutional economist. Reference [6] emphasizes that the development process is not separate and has strong institutional and cultural roots. Economic development has to concern on the strengths of the institutional system of a region. The strategic values of this institutional aspect are institutional change and development will lower the transaction costs and production costs, strengthen trust, and increase learning and interaction. Institutions can affect productivity and influence the development process in turn.

2.2 Rural Development and Financial Sector Institution

In a development perspective, Reference [7] concludes that the economy in Indonesia is divided into two sectors, namely traditional and modern which are not interconnected. It states that the traditional sector needs to be stimulated by the existence of economic incentives and an increase in production technology. On the other hand, states that any kind of improvement efforts will not be successful. Reference [8] states that the problem that applies to rural communities is social rationality which is more concerned with togetherness than competition. External penetration, both in terms of institutional and technological aspects, will create resistance.

All this time, the problem of the rural development process is that there is no institutional development in the economic sector as an instrument to overcome the lack of capital in rural areas. Reference [9] states that the role of institutions in rural development is an entry point in order to establish and accept for an institution, especially in the economic aspect. Revitalization of economic institutions is considered important, therefore this institution can be legitimized again by every individual in it, can foster the sense of belonging, if this sense of belonging appears, each individual will participate and this institution will develop therefore it has the potential to be prosperous for communities because there is already a division of roles and responsibilities in meeting their economic needs.

Based on the developments in rural areas that have occurred over the past few decades, it can be seen that this phase identifies the process of rural commercialization. Efforts are needed in order rural residents can escape from this commercialization, such as by strengthening traditional-based production and processing systems therefore rural communities are not only in a subordinate position. This problem actually can be overcome by the existence of rotating capital in the production and processing system. Limitation of capital is the most complex problem in rural areas. Limitation of capital causes economic activity to not run. The failure of economic activity causes the community to be in a subordinate position [2]. Regarding this situation, it is appropriate for rural development policy makers to marry financial sector institutions with government policies in order to be able to drive economic activities in rural areas, especially micro enterprises.

3. METHOD

Descriptive qualitative method was used for this study. Mostly, the data being used were qualitative data in the form of explanations and descriptions obtained from various sources of literature and related to the role of LPD towards village development. While the sources of the data were obtained from secondary data in the form of notes, documents, journals, books and archives from the results of literature studies or document studies.

4. RESULT AND DISCUSSION

The result of the study found that LPD has a very significant role towards village development in Bali Province. This finding can be explained by the argument that the progress of LPD performance is reflected in the increase of credit amount, the increase in the number of assets and the amount of profit will contribute significantly to the success of village development. The increase of credit amount in LPD will automatically increase the LPD assets and profit potential. If this happens, the LPD capacity and capability will increase in providing services to rural communities. Increasing the ability of LPD to serve the financial needs of the communities will help in increasing the productivity of rural communities. The increase of productivity reflects the potential for the increase of communities' income. The World Bank states that increasing the economic capacity of the communities will ease public access to education and health services.

The increase in the credit amount of LPD reflects an increase in economic capacity and an increase in the self-ability of rural communities. Self-ability here means an increase in people's ability to see opportunities and exploit the potential that is around them. This

means that credit borrowed by the communities is used for productive activities in increasing the income. Increase in income is a reflection of the increase in welfare. When the credit amount in LPD increases, it means that the LPD's trust is getting better for LPD customers. The increase of trust of the LPD in its customers is usually based on obedience to paying instalments punctually. Obedience in paying instalments is largely determined by the financial capacity of the customer. The data shows that the credit amount of LPD continues to increase, which means that the economic capacity of the customers is getting better. If this condition continues, the LPD profit will increase. The credits in this institution are also used for children's education costs. This condition indicates that by achieving a good LPD performance will ease or accelerate the achievement of successful village development in Bali Province. In this regard, it can be understood how meaningful an increase in the amount of profit, the number of assets and the credit amount extended by the LPD to rural communities is.

The story from Grameen Bank inspires how LPD can do more in village development especially in poverty alleviation. The contribution of the LPD in poverty alleviation is believed to be very real. In accordance with the purpose of its establishment, one of which was to eradicate the *ijon* system, slowly but surely, the *rente* system choking economic life in the village is decreasing. LPD grows as a source of funding for micro businesses in rural areas. The development of micro businesses automatically opens job opportunities and in the end it is hoped that the poverty rate will be overcome. One of the growth and development of the creative economy in rural areas is the contribution of the LPD.

The contribution of LPD to poverty alleviation is highly dependent on the profit of its concerned. Conceptually, according to Perda No. 3 Year 2017, the distribution of LPD of remaining profit is mostly enjoyed by the *krama adat* of its village. The increase of the profit percentage of LPD can lead to a reduction in the poverty rate. In the field, it shows that every year LPD profits (20 percent of LPD net profits) are distributed to *desa adat* as the owner. Based on the information in Table 2.1, it is known that from 2008 to 2015 the profit amount of LPD in Bali continued to increase. The increase in profit of LPD will automatically increase the contribution to village development, because the amount that is returned to *krama adat* will also increase. In a period of 8 years, the LPD in Bali has disbursed funds for village development in the amount of 442.46 billion rupiahs, and this figure will increase if it is added to the allocation of LPD funds for social funds. On average, annually, the LPD has contributed to the development of the village as much as 55.31 billion rupiahs.

The profit percentage returned will reduce the *krama* fee to *desa adat*. As is known, the *desa adat* communities annually will pay fees to *desa adat*. The reduction of community burden from these fees allows *krama* to allocate its income to meet other needs such as for children's education costs and for family health. Here, the LPD's performance can directly assist in realizing village development, namely in reducing poor households, increasing the average length of schooling and increasing life expectancy

Table 1. Profit Allocation of Village Micro-Finance Institution in Bali

Year	Profits (billion rupiahs)	For Village Development (billion rupiahs)	Social Funds (billion rupiahs)
2008	131,10	26,22	6,56
2009	151,10	30,22	7,56
2010	188,30	37,66	9,42
2011	232,40	46,48	11,62
2012	276,10	55,22	13,81
2013	331,80	66,36	16,59
2014	407,90	81,58	20,40
2015	493,60	98,72	24,68
Total	2.212,30	442,46	110,62

BPD Bali Bank mentions four positive impacts of LPD for village development, they are: 1) with the existence of the LPD, *desa adat* have received a source of development costs of 20 percent of net income, while other interests come from social funds which are 5 percent; 2) LPD has participated in supporting government programs in poverty alleviation and expanding job opportunities. There are two pathways taken by the LPD in reducing poverty in Bali Province. The first line is LPD supports micro businesses financially, the other one is micro businesses able to create job opportunities and at the same time alleviate poverty; 3) participate in encouraging the growth rate of small industry in rural areas therefore the economic growth of rural communities is getting better; and 4) with the success achieved, the LPD also acts as an object of research on people's economic empowerment.

Socially and religiously, the role of LPD in Bali is very clear. As regulated in Pasal 22 Perda of the LPD regulation, it is stated that the distribution of its net profits at the end of the year will be used, for capital reserves of 60 percent, village development funds is 20 percent, production services is 10 percent, development, supervision and protection funds is 5 percent, and social funds 5 percent. This regulation requires the LPD to contribute 20 percent of the annual profits for the needs

of the village and *banjar adat*. Apart from being used for the physical development of the village and *banjar*, part of the funds obtained from the LPD, by the villagers, is usually used to finance religious ceremonial activities. This means that apart from having a broad economic function, the LPD also has a very high social and religious function throughout Bali. Another tangible contribution made by the LPD was in reducing the cost of the ceremony. There are several LPD that organize the Funeral Contribution Fund program, which the funds can only be disbursed during the *Ngaben* ceremony. The communities were very enthusiastic about welcoming this program because it felt very useful. The community's burden becomes lighter so that it can create silence and holiness in carrying out the ceremony without having to think about excessive funding burdens [10].

The empirical study done by [11] found that Micro Financial Institution is proven to be an approach to alleviating poverty in rural areas because they can provide wider access to the poor who have been unable to access the formal credit market. Micro Financial Institution is also believed to be able to become important tools for realizing development in three ways, namely: creating job opportunities, increasing communities' income, and alleviating poverty. The empirical example of the impact of the success of Micro Financial Institution services, such as in West Java, could be seen from an increase in children's educational participation, an increase in the income of micro entrepreneurs, and an increase in household assets [12]. The success of Micro Financial Institution in Tangerang is identified from the ability of Micro Financial Institution to contribute to Original Local Government Revenue which the volume tends to increase. In 2006, Original Local Government Revenue was paid in the amount of 289 million rupiahs, for 2007 it increased to 600 million rupiahs.

Reference [13] found that the presence of Lumbung Pith Nagari (LPN) Limau Manis in West Sumatra could reduce the activities of Induk Julo (loan sharks) and Julo-julo Tembak (arisan tembak). The presence of this institution had provided alternative options for local residents to obtain safer and more humane loan funds. A culture of saving had also grown among residents, including trust in financial institutions and micro credit, as seen from the high savings of customers at LPN Limau Manis. This fact was emphasized by the Chairperson of the Kerapatan Adat Nagari (KAN) Limau Manis, Wardas Tanjung, that the social impact of the LPN on household income levels, house renovation, children's education level, household health level, wage labours in the household were quite significant. In short, the presence of LPN Limau Manis had raised the welfare level of the Limau Manis residents.

In the economic system, the concept of microfinance is considered appropriate for village development [13]. According to Asian Development Bank, microfinance is a number of financial services such as deposits, loans, payment services, money transfers and insurance for the poor and low income family groups as well as for their micro businesses. From this definition, microfinance is as opposed to macro finance which is controlled by the market by prioritizing financial and credit services based on the needs of the communities. In addition, microfinance also prioritizes values of the society, such as altruistic values, therefore it is also often referred to as the community economy. The morality aspect of this microfinance is partly evoked by religious movements in Africa and Asia as a critique of the immorality of western economies which had resulted in lecherous homo economicus. Microfinance prioritizes the values of self-integrity, morality and economic independence. The success of Grameen Bank (GB) in Bangladesh opened the world's eyes to the importance of microfinance for poverty alleviation and peace making. Many people see the GB model as a model for a successful approach to poverty alleviation and increasing the role of women so that many parties had implicated the GB method. The GB pattern replication in Indonesia took place in 1989 in Nanggung, West Java, initiated by the Puslitbang Sosek Pertanian Badan Litbang Pertanian (Agricultural Agency). Further management was carried out by the Independent Business Development Foundation (YPKUM). Subsequent replications were carried out in several other areas such as Tangerang, in the tidal areas of South Sumatra, South Sulawesi, East Java, and other places that had not yet been identified.

5. CONCLUSION

The LPD plays a significant role in village development. This means that the success of the LPD will determine the success of village development in Bali Province. Based on the results of the study, there are several suggestions that can be submitted. First, it is suggested to the LPD administrators to maintain public trust by showing a professional attitude that upholds the values of honesty. The trust of communities will determine community involvement / participation in programs implemented in rural areas, such as active participation in supporting the performance progress of LPD and realizing the success of village development. Second, it is suggested to government agencies that they should pay serious attention to the existence of the LPD as a financial institution that grows and develops in rural areas. It is important to provide training and coaching in a tiered and continuous manner to administrators and parties involved in LPD management to maintain the existence of LPD

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