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Model of Capital Structure For Small and Medium Enterprises in Bandung City

Nenden Kostini
Faculty of Social and Political Science
Universitas Padjadjaran
Jatinangor - Sumedang, Indonesia
nenden.kostini@unpad.ac.id

***Abstract*—Small business capital is limited in number and access to funding sources. The right composition of debt and capital can form an optimal capital structure. The purpose of this study is to examine factors associated with the capital structure of Small Business in Bandung; and to formulate a model of capital structure of Small Businesses in Bandung City. The sample of this research is 100 small business in Bandung City. Based on the findings, factors such as firm size, company growth, profitability, liquidity, asset structure and the form of legal entity forming the capital structure of small businesses in Bandung City.**

Keywords: firm size; company growth; profitability; liquidity; assets structure; capital structure

I. INTRODUCTION

As we all know, small and medium enterprises, or better known as SMEs, has made a great contribution to the Indonesian economy. Ranging from employment to the increase in gross domestic product. Employment by SMEs reached 97.16 percent, or about 107 million people working in the SME sector, and the gross domestic product, SMEs contributed 59.08 percent [1]. In other words, the role of SMEs in Indonesia cannot be denied and underestimated.

In times of economic crisis, SMEs can survive, while on the other hand many large businesses that have failed. This is not another because, in general, SMEs are growing in Indonesia is a business engaged in the sectors that produce consumer goods and services, which are needed by the community. In addition, the other reason is SMEs generally utilize local resources, both for human resources, capital, raw materials, to the equipment. That is, most SMEs do not need to rely on imported goods. And the latter is generally not supported by the SME business loan from a bank, but from its own funds.

Although the number of SMEs from year to year has increased but SMEs still face many obstacles and problems that are relatively the same. The obstacles include access to finance, access to markets, technology and innovation, as well as consulting services and information. Constraints in access to finance faced among others, (1) doubt the banks to lend to SMEs, especially for entrepreneurs and innovative SMEs; (2) the obligation to use collateral on the loan; (3) Institute of credit guarantees no or limited; (4) the majority of SMEs depend on the informal financial institutions.

Many aspects that can affect the development of SMEs. One of them already mentioned above is a capital aspect. Capital aspect related to the source of funds that should be available to be utilized as capital that can support production. As known, the SME capital sourced from internal capital, ie from the owner. However, because their numbers are limited so when the greater capital requirements, SMEs must find alternative sources of external funding, which one of them is with debt (debt financing).

Decision-making about the appropriate funding sources, consisting of debt and equity used to finance the company's assets, it is vital for companies to achieve financial balance. An establishment is in a state of financial balance, if the firm for carrying out its functions do not face financial disruption, which caused an imbalance between the amount of capital available to the amount of capital needed [2].

Therefore, the need for an optimal balance between the two sources of funds. Companies are expected to have the amount of debt that is greater than the amount of their own capital, or in other words, a debt ratio of not greater than 50%, so that capital is guaranteed (the debt) is not greater than the capital that collateral (equity). Based on the theory, the optimal capital structure can be achieved when the amount of debt does not exceed the equity capital of the company, or at least the composition of 1: 1 or 50% long-term debt and 50% equity. Because of the large capital costs and risks faced from external funding depending on the proportion of each source of funds as well as the cost of each source of funds [3]

The funding decision the company will determine the company's ability to perform activities of the company's operations and also against the risk of the company itself [4]. This is also confirmed by the opinions which states that this type of funding decisions is vital to a company's financial well-being. The wrong decision on capital structure can lead to financial distress and ended in bankruptcy [5]

Research conducted in the city of Bandung, which is on the small and medium enterprises. Since 2000, SMEs in Bandung continues to grow. This shows that SMEs in Bandung still have the opportunity to continue to grow and develop.

Corresponding author: Nenden Kostini

When linked to the problems faced by SMEs, namely capital aspect. Obviously, this is very interesting to study. Because on the one hand capital constraints SMEs face, but on the other hand precisely the number of SMEs continues to grow.

II. RESEARCH METHOD

This study utilized a quantitative, explanatory survey method which aims to interpret the relationship between variables by interpreting the results of hypothesis testing. The population of this study is a small business recorded on the Office of Cooperatives, small and medium enterprises Bandung City as many as 4.531 small and medium enterprises, and taken as a sample of research as many as 100 small businesses [6]. And, for data analysis technique used multiple regression analysis, then testing simultaneous and partial hypothesis.

The aims of this study is to determine the factors that affect the model of capital structure of small businesses in the city of Bandung. These factors are firm size, company growth, profitability, liquidity, asset structure and a dummy variable, a business legal entity.

The size of the firm is based on the natural log of total assets, the growth of the company based on the sales growth, profitability is measured by ROE, while the asset structure is measured by total assets, and the legal entity is viewed based on whether the small business is incorporated or not.

The data collected for the analysis in this study based on the financial statement information of the small business concerned. Financial statement data collected consists of the amount and type of assets, debt and capital, and sales.

III. RESULT AND DISCUSSION

Factors that influence the model of capital structure of small-scale business in Bandung, consist of firm size, company growth, profitability, liquidity, asset structure, and a dummy variable, small business legal entity. These factors are also called company characteristics. Company characteristics basically reflects the fundamental condition of the company. The determination of the characteristics of the company can be determined by using three categories, namely: the characteristics associated with the structure (structure), performance (performance), and the market [7].

The structure includes sizes (size) of the company, and the company's ability to repay obligations or leverage (the company's solvency). Then the performance includes the company's ability to fund its operations and repay short-term liabilities (liquidity of the company) and the company's ability to generate earnings (the company's profitability). Furthermore, market-related characteristics, determined by factors that are qualitative, for example, the guaranteed value of assets or asset structure (tangibility).

Furthermore, the study variables frequently associated with the characteristics of the company is its capital structure. The differences in the characteristics of the company will lead to differences in the composition of the capital structure and funding sources fulfillment of decisions of the company [8]. Characteristics of the company can influence the decision of the fulfillment of the source of funds of companies and the level of debt the company [9].

Model relationships between these variables can be arranged in a function or equation as follows:

$$LDER = -0{,}113LCR + 2{,}924LROE - 3{,}027LSG + 0{,}595LSIZE - 0{,}165LTANG - 0{,}015BH \quad (1)$$

The results showed that the variable coefficient for liquidity in the regression equation is -0.113 which means that the effect of liquidity on the capital structure is negative. This means that the higher the liquidity the capital structure will decrease. High liquidity means that the company is able to cover the obligations that are due in time. For SMEs, the excess cash available can be a source of capital for operational activities. The amount of cash held by SMEs will encourage SMEs not to seek additional funds or capital from outside parties. Thus, SMEs do not seek additional capital from outside parties and able to meet its obligations, indirectly the amount of debt SMEs will be reduced.

High profitability of SMEs means that SMEs earn a large profit from operational activities. However, because the management is still not good, especially in terms of financial management, SMEs difficulty in managing the profits obtained. Based on the results of interviews with some respondents note that in operational activities, production operational costs are not distinguished from the daily household expenditure. This means that profits or profits derived from operational activities are also used for household expenditure. The greater the profits or profits earned then the profit or profit is considered as excess cash that can be used. Thus, the amount of profit that SMEs do not make it as a source of capital or internal funds, so to cover the shortage of operating costs are met by way of seeking a loan. This makes the debt rate also become larger.

The result of data processing shows that growth variable of company by using measure of sales growth (Sales Growth), has regression coefficient value -3,027. This negative value can be interpreted that there is a negative effect of sales growth on Debt Ratio SMEs in Bandung. Negative value can also be interpreted as a relationship that is directly proportional to the upside, the higher the sales growth the lower the level of debt or vice versa. In other words, the growth of the company negatively affects the capital structure of small and medium enterprises. The results of this study are different from the hypothesis of this research that predicts that the growth of the company has a positive effect on capital structure. In general, when companies experience increased sales growth then it will make the company become more stable. Under these conditions the company can operate by not relying on sources of capital from outside the company. Because high sales growth can be an indication that the company's revenue also increases. But this condition is different from that found in SMEs in the city of Bandung. High corporate growth is defined as additional revenue for SMEs. However, due to the unfinished functioning of the financial function, namely the separation of business functions and the personal / family financial function, the expenditure for personal / family is not

separated from business expenses. This causes the problem of lack of capital for the next production activity. And as a way out, SMEs will look for alternative sources of other funds, namely with debt. This condition is, which can explain why the research hypothesis is different from the hypothesis proposed in advance. The results of this study can also be related to the pecking order theory, which states that the company will first use internal funds (retained Earnings) to finance its investment because the cost of Fund of internal funds is the cheapest. If internal funds are not sufficient, then will use the financing with debt. While financing with equity is the last alternative because it is considered to cause the highest cost of fund. The tendency to support pecking-order theory in small business capital structure policy is evident from the financing structure which tend to be used by small business that is using internal fund to finance its investment, compared with debt financing.

Based on result of regression equation seen that coefficient of variable of firm size is +0,595. The coefficient of variable marked (+), it can be concluded that the size of the company has a positive effect on capital structure, in other words that the higher the size of the company the higher the rate of debt. The effect of firm size on this capital structure was significant so that the result of this regression in accordance with the hypothesis of the study predicts that firm size has a positive and significant influence on capital structure. The results of this study are in line with the theory of trade-offs that link the use of large debts with increased risk of bankruptcy. The trade-off theory suggests that large firms tend to be more diversified, so the risk of going bankrupt is negligible with small firms so large firms tend to have higher debt ratios [8].

The results showed that partially asset structure has no effect on capital structure. This is different from the hypothesis proposed in this study, the asset structure has a positive effect on capital structure. A company with sufficient assets or greater fixed asset composition will use more long-term debt. This is because the fixed assets will be used as collateral for its debts. This means that debt can be determined based on the size of existing fixed assets. But unlike the case faced by SMEs in the city of Bandung. Most SMEs get debt in the form of short-term debt and the amount has been determined by the bank or other financial institutions. On the one hand, fixed assets are owned as collateral but on the other hand the fixed asset amount is not used as a measure of size to get a large amount of debt. So that this can explain the existence of a negative relationship between the structure of assets with capital structure. In addition, the results of this study can explain the financial behavior of small businesses that often experience bankruptcy due to borrowing to external parties in a certain number of relatively large amounts. This means that the amount of assets used as collateral to obtain the loan is not comparable, so that the direct impact when the small business actors cannot repay the loan and eventually went bankrupt.

Table 1. The result of the F-statistic Capital Structure

F-statistik	Level of signifikan	Prob (F-statistik)
72.70207	Sig in α = 0.05	0,0000

The estimation results of the model equations Capital Structure demonstrate the value of test F-statistic of 72.70207 with a probability of F-statistics of 0. The Ftable obtained amounted to 2.20 (with DF1 = 6; DF2 = 94; α = 5%).

Thus, it can be seen that the value of F-statistic of 72.70207> 2.31 (F-table) and a probability value of F-statistics of 0.0 <0.05 (F-table). Based on these results, a decision that can be taken is H0. By rejecting H0, meaning it can be interpreted that the variable firm size (SIZE), liquidity (Cash Ratio), sales growth (Sales Growth), profitability (ROE), the structure of assets (TANG), and legal entities (LE) effect simultaneous to variable capital structure (DER) of SMEs in Bandung.

Based on the test results of this research can be known variables that make up the capital structure of SMEs in the city of Bandung is firm size, the company's growth and profitability. Firm size affects positively on the capital structure. The larger the size of the company it will be easier for businesses to obtain the debt. This means that the size of the company can be used as a basis for determining the amount of the debt to be obtained. Small-scale enterprise will acquire a debt that is less than the large-scale enterprise.

While the growth of the company, in this study was measured using the sales growth, the results showed that had a negative effect on the capital structure. Companies that have increased the value of sales always have the confidence to not obtain loans from external parties. Due to the high sales show that they have a source of internal funding, which comes from income, which could be used to guarantee the operational fund operations. So as a source of funding from external parties, namely in the form of debt is no longer needed. With sales growth continues to increase, the debt is not required so that the numbers will continue to decline. Therefore, it can be said that the company's growth can be used as variables that determine the company's capital structure, particularly on SMEs in Bandung.

And lastly, the variables that can determine the capital structure is profitability. By looking at previous descriptions that companies with high sales growth will generate higher profits anyway. Increasing profit would be an indicator of success of the companies concerned so as to enhance the confidence of creditors to continue providing loans. The larger the profits, the acquisition debt provided will be greater. This is considered as a basic bias that profitability is a variable that can determine the capital structure of SMEs in the city of Bandung.

IV. CONCLUSION

Factors that may determine the capital structure of SMEs in Bandung consisting of firm size, company growth, and profitability. The influence of the variable firm size, liquidity, growth, profitability, asset structure and legal entities on the capital structure included in the category of strong influence

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