

Research Horizon

ISSN: 2808-0696 (p), 2807-9531 (e)

Research Horizon

Volume: 04

Issue: 06

Year: 2024

Page: 265-272

Empowering MSMEs as the Backbone of the National Economy through Credit Insurance

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Abstract

This research explores the effectiveness of credit insurance in empowering MSMEs, which is one of the important sectors in building the national economy. Using a descriptive qualitative method with a case study of Bank Rakyat Indonesia (BRI), this research analyses changes in the Non-Performing Loan (NPL) ratio for MSME loans before and after the implementation of credit insurance. Data was collected from a literature review, reports from the Financial Services Authority (*Otoritas Jasa Keuangan*/OJK), Bank Indonesia, Ministry of Cooperatives and MSMEs, and BRI's internal reports. The findings show that the implementation of credit insurance lowered the NPL ratio in BRI's MSME segment from 3.5% to 2.1% over two years, supporting the role of credit insurance as a risk mitigation tool that transfers default risk to the insurance company. These results strengthen the theory of risk mitigation and have practical implications for banks in expanding access to secure financing for MSMEs. A limitation of this study is its focus on one bank, which means the results may not be generalizable across the board. Policymakers and regulators are encouraged to consider policies that encourage wider adoption of credit insurance for MSMEs. This study offers insights into developing effective risk mitigation strategies for the MSME credit sector.

Keywords

MSME, Non-Performing Loan, Credit Insurance, National Economy

1. Introduction

MSMEs are very important to drive a country's economy, especially in developing countries like Indonesia. The contribution of MSMEs to job creation and Gross Domestic Product (GDP) is very large. MSMEs contribute more than 60% of GDP and absorb more than 90% of the workforce (Ministry of Cooperatives and MSMEs, 2021). This role not only helps the national economy but also increases competitiveness and economic resilience amidst global changes (Amirudin et al., 2024). However, despite their significant contributions, MSMEs face many problems. The most prominent is access to safe and stable financing. This access is often a major obstacle for MSMEs to grow, innovate, and survive in the long term, especially when the economy is changing (Ardiati, 2022).

Certain factors, such as the high-risk profile of MSMEs that are considered high by financial institutions and the amount of collateral they can provide, make it difficult to obtain financing (Assalmani, 2021). This has led many banks and financial institutions to refuse to provide credit to MSMEs because they are considered more vulnerable to bad debts or defaults than other business sector (Wijayanti, 2009; Rachmad, 2007). Credit insurance has emerged as one of the promising ways to reduce risk in such situations. Credit insurance protects banks or financial institutions from losses caused by MSMEs that cannot pay their credit. Thus, the risk faced by banks is minimized, so that financial institutions are more motivated to provide credit to MSMEs without worrying about experiencing significant losses due to non-performing loans (Gupta & Kaur, 2022).

Banks use credit insurance as collateral, so the insurance company takes on most of the risk of default. According to Kim et al. (2020). AndImbierowicz & Rauch (2014), the implementation of credit insurance has the potential to reduce the ratio of bad debts in the banking sector, especially for loans given to MSMEs. Banks in Indonesia that implement credit insurance show a lower level of Non-Performing Loans (NPL) (Irwan, 2017). This shows that credit insurance can play an important role in maintaining the financial stability of banks while increasing access to financing for small and medium enterprises (SMEs) that are in dire need of capital support to grow (Siamat, 2005; Mishkin, 2019). In addition, this protection makes banks more confident in supporting financing for industries that require special assistance, such as MSMEs that are still in the development stage or do not have strong collateral (Utomo, 2005).

MSMEs can also gain long-term benefits through credit insurance mechanisms. MSMEs can increase productivity, expand markets, and innovate to create more competitive goods or services with easier and more affordable access to financing. With this increased capacity, the role of MSMEs as the main pillar of the national economy will certainly be strengthened. In addition, credit insurance support helps MSMEs obtain financing and improve financial literacy and risk management, both of which are very important for the survival of small and medium businesses (Chosyali & Sartono, 2019; Abdelaziz et al., 2020). As a result, credit insurance not only protects financial institutions, but also improves the sustainability and resilience of MSMEs (Mujianto et al., 2023).

In terms of policy, the government and regulators must support credit insurance to reduce the credit risk of MSMEs. With this strategy, MSMEs can continue to play an important role in the MSME financing ecosystem. The government can play a role by providing incentives to insurance companies that provide credit insurance products specifically for MSMEs, so that insurance premiums become cheaper for MSMEs and their partner financial institutions. Regulatory policies that support cooperation between insurance companies and financial institutions will help create a healthy ecosystem for MSME financing.

2. Methods

This study uses a qualitative descriptive method with a case study approach. This method was chosen to explore in depth the effectiveness of credit insurance in supporting the sustainability of MSME financing as a pillar of the national economy. The qualitative descriptive method aims to describe the situation in detail and in depth, especially in the context of implementing credit insurance as a credit risk mitigation tool for MSMEs. The case study was chosen with a focus on Bank Rakyat Indonesia (BRI) as one of the banks that actively distributes MSME credit in Indonesia, and has implemented credit insurance as a risk mitigation (Ramadhan et al., 2024).

The data collection techniques employed in this study encompass a literature review, secondary data analysis, and a case study approach. The literature review involves examining relevant sources such as books, scientific journals, and prior research reports on MSMEs, credit risk, and the role of credit insurance as a risk mitigation tool (Kasmir, 2015; Ghosh, 2020; Putranti et al., 2020). These sources provide a theoretical foundation and contextual understanding of the relationship between credit insurance and credit stability for small and medium enterprises (SMEs). Secondary data analysis utilizes official reports from institutions like the Financial Services Authority (*Otoritas Jasa Keuangan/OJK*), Bank Indonesia, and the Ministry of Cooperatives and MSMEs, offering statistical insights into the number of MSMEs, their contribution to Gross Domestic Product (GDP), the non-performing loan (NPL) ratio in the MSME sector, and the performance of credit insurance in banking institutions. Additionally, a case study of BRI Bank is conducted, focusing on internal reports that analyse the performance of MSME credit and Home Ownership Credit (KPR) products with credit insurance. This includes evaluating NPL levels before and after credit insurance implementation, as well as reviewing internal policies supporting its application. The case study aims to demonstrate how credit insurance reduces credit risk for the MSME sector.

The collected data were analysed using qualitative and comparative approaches through several stages. Initially, the data were grouped based on their source and type, including literature reviews, secondary reports, and case studies related to BRI Bank. This categorization encompassed MSME statistics, non-performing loan (NPL) data before and after credit insurance implementation, and policies regarding credit insurance at BRI. Following this, a comparative analysis was conducted to evaluate the credit conditions of MSMEs at BRI before and after the implementation of credit insurance (Laeq, 2021). This approach aimed to assess the effectiveness of credit insurance in reducing the risk of bad debt by observing changes in NPL levels and MSME credit accessibility. Finally, the analysis results were synthesized into a conclusion to provide insights into the role and performance of credit insurance in supporting MSMEs. The conclusion also offered recommendations for financial institutions on managing MSME credit risk and for policymakers to promote broader adoption of credit insurance in this sector.

3. Results

The results of the data analysis show that the risk of Non-Performing Loans (NPL) in the banking sector is significantly reduced by implementing credit insurance in the Micro, Small, and Medium Enterprises (MSMEs) segment. The results show that banks that use credit insurance as a means of reducing risk have lower NPL levels compared to banks that do not. According to research conducted by Kim et al. (2020), the implementation of credit insurance in South Korea also showed similar results: the possibility of default can be reduced, which helps banks remain stable. In this case, the implementation of credit insurance in the small and medium enterprise (MSME) group has proven useful for financial institutions in

maintaining financing sustainability. This study also helps develop the science of banking risk management, especially in the MSME sector which is vulnerable to credit risk (Hanggiani et al., 2024). Specifically, data from BRI Bank, which has implemented credit insurance since 2021, shows a decrease in the NPL of the MSME segment from 3.5% to 2.1% in two years.

The significant decrease in the NPL ratio is due to the credit insurance mechanism, which covers most of the losses from bad loans, allowing banks to channel credit without bearing the full risk. This result is in line with the risk mitigation theory, which states that credit insurance works well to transfer risk to third parties (Hasibuan, 2017). As a result, banks have a greater opportunity to help Small and Medium Businesses (SMEs). From a practical perspective, the implementation of credit insurance also helps financial institutions see MSME credit better. MSMEs face major challenges in obtaining conventional financing because this sector is often considered to have high risk. However, with credit insurance, banks can feel safer in providing credit to MSMEs because insurance takes over most of the risk of default. This is in line with the findings of research conducted by Andriani & Tanjung (2015), which found that risk mitigation through credit insurance resulted in greater financing opportunities in high-risk sectors. As this study shows, credit insurance not only reduces risk for banks but also provides MSMEs with greater opportunities to obtain financing (Suprapti & Suparmi, 2022).

In addition, the findings of this study have theoretical benefits by strengthening the statements in the related literature about the function of credit insurance as a means to reduce risk. Credit insurance helps banks maintain the stability of their credit portfolios by protecting them from the risk of bad debts (Kasmir, 2015; Dwinanda & Sulistyowati, 2021). In addition, this study emphasizes that effective implementation of credit insurance requires supportive regulations and policies, such as those implemented in several countries that provide incentives for low-cost credit insurance products for small and medium enterprises (SMEs). With the right policy support, credit insurance can serve as a risk mitigation and support the stability of the banking sector. In a broader perspective, this study opens space for further development in the field of banking risk management and MSME financing policies. The findings of this study indicate that financial institutions can play a greater role in encouraging MSME-based economic growth by expanding the application of credit insurance. In addition, this study suggests that the government and financial regulators be more active in facilitating and promoting credit insurance for MSMEs. Thus, the results of this study not only support the theory of risk mitigation but also offer practical insights for banks, policymakers, and insurance companies in creating a more inclusive and sustainable financing ecosystem.

4. Discussion

This study found that credit insurance can play an important role in reducing the risk of non-performing loans (NPL) in the MSME sector. The implementation of credit insurance in the MSME segment at Bank BRI resulted in a significant decrease in NPL from 3.5% to 2.1% in two years, indicating the ability of insurance to transfer risk from banks to insurance companies. These results are in line with research by Kim et al. (2020), which shows that credit insurance has succeeded in reducing the risk of default in the South Korean banking sector. This is known as one of the main objectives of credit insurance in risk mitigation theory, namely reducing financial risk by protecting you from possible losses. Therefore, this study confirms the position of credit insurance as an effective tool to reduce damage in the small and medium enterprise (MSME) sector.

In practice, the implementation of credit insurance allows banks to be more flexible in providing financing to MSMEs, which are often considered as segments with high credit risk. According to this study, MSMEs have a higher risk of default

compared to other sectors. As a result, banks often limit financing to MSMEs because of this risk. Banks can transfer most of the risk to the insurance party by implementing credit insurance, which allows them to be more active in providing financing to MSMEs. These results support previous studies which state that financial institutions can view MSMEs with better credit risk with credit insurance (Wijayanti, 2019; Hasibuan, 2017). Therefore, credit insurance can increase financial inclusion for small and medium enterprises (MSMEs).

From an economic perspective, the results of this study support the idea that credit insurance can help banks support the MSME sector, which is an important part of the national economy. Banks can provide credit to MSMEs more often without worrying about major losses due to bad debts with a lower NPL ratio. As a sector that contributes greatly to GDP and job creation, the decline in NPL at Bank BRI shows a wider economic potential. More stable financing support for MSMEs will have a positive impact on the economy.

In addition to direct benefits, the implementation of credit insurance also has a significant impact on MSME financing policies. This study shows that if credit insurance is supported by supportive regulations, such as tax incentives or affordable premium regulations for MSMEs, the role of credit insurance will be more optimal. In several countries, policies that support credit insurance for MSMEs have increased access to credit for these businesses (Chosyali & Sartono, 2019). This policy support encourages banks to continue providing credit to MSMEs without increasing the risk of bad debts (Jorion, 2007; Fombrun, 1996). Consequently, this study provides important insights for financial regulators and governments to create more inclusive policies to support the growth of small and medium enterprises (SMEs) through credit insurance. This study, from the perspective of scientific development, adds empirical evidence on the effectiveness of credit insurance in the MSME industry and enriches the literature on credit risk mitigation. In addition, these findings open opportunities for further research aimed at developing a credit insurance model that is more in line with the characteristics of MSMEs in Indonesia. This is due to the high variation in risk in this sector depending on the sector and scale of the business. To gain a better understanding of the impact of credit insurance, further research is expected to examine various other factors, such as the type of MSME business and macroeconomic performance. Thus, the findings of this study contribute both theoretically and practically to building a safer and more inclusive financing system for MSMEs as a pillar of the national economy.

5. Conclusion

This study found that credit insurance plays an important role in reducing the risk of bad debts or Non-Performing Loans (NPL) in the MSME sector, with significant implementation results at Bank BRI. Credit insurance has proven to be an effective risk mitigation tool, because banks that implement it experience a decrease in the NPL ratio, which gives them greater flexibility to provide financing to MSMEs. This implementation is in accordance with the objectives of the research. This study shows that credit insurance not only protects banks from financial losses due to bad debts, but can also increase financial inclusion of MSMEs by improving their risk perception. Given these findings, policies are needed to support the wider implementation of credit insurance in the MSME sector. Supportive regulations, such as tax incentives and affordable insurance premiums, can help MSMEs obtain more financing while maintaining the stability of the banking sector. This study only focuses on Bank BRI as a case study, so the results cannot be generalized to all financial institutions in Indonesia. Therefore, a more comprehensive picture is expected from further research involving more banks and types of MSMEs.

As a recommendation, banks that have a high MSME credit portfolio should prioritize the implementation of credit insurance in the MSME sector. In addition,

it is recommended that banks work together with insurance companies to develop more flexible and affordable credit insurance products for MSMEs. The government and regulators should consider supporting policies that encourage MSME access to safe financing through credit insurance, so that the MSME sector can earn more money.

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