

**SMALL AND MEDIUM ENTERPRISES (SMEs)
PERFORMANCE IN ACEH JAYA, INDONESIA**

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**SMALL AND MEDIUM ENTERPRISES (SMEs)
PERFORMANCE IN ACEH JAYA, INDONESIA**

by

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LIST OF ABBREVIATIONS

ABS	Australian Bureau of Statistic
BC	Bolton Committee
<i>BI</i>	<i>Bank Indonesia/Indonesia Bank</i>
<i>BPS</i>	<i>Badan Pusat Statistik/Central Bureau of Statistics</i>
CB	Community Businesses
CC	Counseling Certificate
CCDSI	Coodinating Council for Development of Small-Scale Industries
CED	Committee for Economic Development
CFI	Comparative Fit Index
CGC	Credit Guarantee Corporation
CMIN/DF	Minimum Discrepancy
CMP	Current Market Prices
CMP	Constant Market Prices
DB	Domestic Brands
DF	Degree of Freedom
EC	European Commission
FB	Foreign Brands
FDI	Foreign Direct Investment
GD	Geographic Diversity
GDP	Gross Domestic Product
GLS	General Least Square
GOF	Goodness of Fit
HSBC	Hongkong and Shanghai Banking Corporation
<i>Inpres</i>	<i>Instruksi Presiden/Presiden Instruction</i>
IPO	Initial Public Offering
ISO	International Organization for Standardization
<i>Keppres</i>	<i>Keputusan Presiden/Presiden Decree</i>
LB	Large Business
LE	Large Enterprise
LSDV	Least Square Dummy Variable
MDA	Multiple Discriminant Analysis
<i>Menkeu</i>	<i>Menteri Kewangan/Ministry of Finance</i>

<i>Menkes</i>	<i>Menteri Kesehatan/Ministry of Health</i>
<i>Menkop</i>	<i>Menteri Koperasi/Ministry of Cooperative</i>
<i>Menperind</i>	<i>Menteri Perindustrian/Ministry of Industry</i>
MITI	Ministry of Trade and Industry
MNEs	Multinational Enterprises
NI	Net Income
NID	National Interest Deduction
NIEs	Newly Industrialized Economies
NN	Neural Network
ODOI	One District One Industry
OLS	Ordinary Least Square
OPC	OTOP Product Champion
OSMEP	Official Small and Medium Enterprises Promotion
OTOP	One Tambon One Product
OVOP	One Village One Product
PD	Product Diversity
<i>RI</i>	<i>Republik Indonesia/Republic of Indonesia</i>
RMSEA	Root Mean Square Error of Approximation
ROA	Return on Asset
ROE	Return on Equity
ROI	Return on Investment
ROS	Return on Sales
<i>RPJPN</i>	<i>Rencana Pembangunan Jangka Panjang Nasional/Long-Term of National Development Plan</i>
SBA	Small Business Administration
SMEs	Small and Medium Enterprises
SMIDEC	Small and Medium-Sized Industry Development Corporation
SIV	Survival Index Value
SPI	Survival Progression Indicator
SRMR	Standardized Root Mean Squared Residual
TLI	Tucker Lewis Index
TMT	Top Management Team
UK	United Kingdom
<i>UKM</i>	<i>Usaha Kecil Menengah/Small and Medium Enterprise</i>
US	United States
USDA	US Department of Agriculture

PRESTASI PERUSAHAAN KECIL DAN SEDERHANA (PKS)

DI ACEH JAYA, INDONESIA

ABSTRAK

PKS di Aceh Jaya memainkan peranan penting dalam pembangunan ekonomi tempatan mengenai penjanaaan pendapatan, kemiskinan, dan peluang pekerjaan. Tetapi pada masa ini, PKS menghadapi saingan yang hebat dalam pasaran tempatan dan dasar kerajaan yang tidak membantu kepada pertumbuhan PKS. Oleh itu prestasi PKS adalah penting untuk menentukan kelangsungan PKS. Justeru kajian ini bertujuan untuk mengukur prestasi PKS di Aceh Jaya, menilai ciri-ciri pemilik dan perniagaan dalam mempengaruhi prestasi PKS dan mengukur struktur hubungan pembolehubah prestasi PKS. Seramai 260 pemilik PKS terlibat dalam penyiasatan kajian. Survival Indeks nilai (SIV) dibangunkan oleh Abouzeedan dan Busler (2004) merupakan ukuran utama PKS di Aceh Jaya. Dapatan kajian mendapati bahawa 84.23(%) daripada PKS di Aceh Jaya melaporkan prestasi yang baik, 12.31(%) melaporkan prestasi yang sederhana dan 3.46(%) melaporkan prestasi yang lemah. Analisis Ordered logit menunjukkan bahawa jantina, kemahiran, teknologi yang digunakan dan jenis bantuan secara signifikan mempengaruhi prestasi PKS. Analisis SEM menunjukkan bahawa teknologi yang digunakan secara signifikan mempengaruhi prestasi PKS melalui bidang perniagaan. Kajian ini menyarankan kepada kerajaan Aceh Jaya supaya mempertingkatkan dan mempelbagaikan jenis bantuan kepada PKS supaya mereka boleh bersaing dalam pasaran tempatan. Bagi membantu dari segi teknologi yang digunakan, kerajaan perlu mengambilkira bidang perniagaan yang diusahakan oleh PKS.

SMALL AND MEDIUM ENTERPRISES (SMEs) PERFORMANCE IN ACEH JAYA, INDONESIA

ABSTRACT

SMEs in Aceh Jaya plays prominent role in the development of local economy with regard to income generation, poverty eradication, and employment opportunities. But at present, SMEs are facing vast competition within the local markets and unfavorable government policy towards SMEs growth. As such SMEs performance are essential to determine the livelihood of SMEs. Hence, this study aims to measure the performance of SMEs in Aceh Jaya, assess owners and business characteristics in influencing SMEs performance and measure structural relationship of variables on SMEs performance. 260 SMEs owners were involved in the study survey. Survival Index Value (SIV) prescribed by Abouzeedan and Busler (2004) was the main measurement of SMEs in Aceh Jaya. It was found that 84.23(%) of SMEs in Aceh Jaya reported good performance, 12.31(%) reported moderate performance and 3.46(%) reported poor performance. Ordered logit analysis indicated that gender, skills, the technology used and type of assistance significantly influence SMEs performance. The SEM analysis indicated that technology used significantly influence SMEs performance through the business field. The study recommends to the Government of Aceh Jaya in order to enhance and diversify the types of assistance to SMEs so that they can compete in the local market. For help in terms of technology used, the Government should take into account the business undertaken by SMEs.

CHAPTER 1

INTRODUCTION

1.1. Background of study

Small and Medium Enterprises (SMEs) are a group of businesses largely owned by lower middle-income communities as a source of income for survival. Most of them successfully survived when the economic crisis hit Indonesia. Instead of high survival during the crisis, the business proactively created new jobs for communities and contribute to solving the problems of unemployment and poverty alleviation. This study aims to measure the performance of SMEs in Aceh Jaya to find contribution factors that influence the performance of SMEs businesses.

1.2. Importance of SMEs to Indonesia Economy

SMEs plays a significant role in the national economic growth in Indonesia. Theoretically, SMEs contribute a high share to the national GDP despite low productivity caused by the low output growth compared to large enterprises. However, currently in Indonesia, the SMEs's journey are facing unfavorable situation due to differences in regulation and policies of the government which limits the SMEs movement to access resources thus unable to accommodate the beginners. To make things worse, it is also compounded by the government's inconsistency of foreign policy in SMEs development. In one point, the government protects SMEs to be able to evolve, however, on the other point, the faucet of import policy opened for goods which can be produced by the local SMEs with lower prices can trigger a fierce price competition. These situations may bring a lot of disadvantages to SMEs.

The low productivity of SMEs is caused by few factors, such as awaiting for the successful development of the local product through OVOP movement, few problems related to the development of SMEs products and lack of marketing strategies and support from relevant agencies to increase products value-added. In addition, the global competition is increasingly threatening where majority of SMEs in Indonesia yet to have an adequate ability in producing goods to compete in the global market and fulfil the needs of ASEAN Free Trade (AFTA), ASEAN China Free Trade Area (ACFTA) launched in 2010 and Asean Economic Community (AEC) (2015).

1.3. General Definition of SMEs

Small and Medium Enterprises (SMEs) are integrated economic entity within an economic system having a strategic potential to strengthen national economic development. Usually, the entity operates individually, groups or in firms in informal sectors where those are not a subsidiary or branch of other firms. Recently, SMEs have become one of the economic actors in providing the community income and employment. In developing countries like Indonesia, SMEs are often linked to cope socio-economic problems such as poverty, unemployment, inadequate income, and gaps between rural and urban development. SMEs are gaining the attention of multiple stakeholders, both from the government and non-government organization (NGO) as an alternative to economic development. With the SMEs growth, it is expected to be able to overcome abovementioned problems.

A few to mention, there are several advantages of SMEs either in developed or developing countries such as high ability in absorbing workforce and production of diversity products of goods and services with high economic values. A survey conducted by the United Nations (1993) stated that SMEs play a significant role in

the economic and social structure in developed economies and dominating more than 90(%) of whole enterprises in developing countries. The survey was strengthened by the research conducted by Hashim and Abdullah (2000), Qian (2002), Ahlstrom, Bruton, and Yeh (2008), Yang et al. (2009). They found that SMEs operates in almost every field of industrial and manufactures sectors. Meanwhile in Asian countries, SMEs are more dominantly engaged in primary sectors such as agriculture, processing, and services. Based on few researches carried out in some other Asia countries such as Thailand, India, Vietnam, and Malaysia, it is proved that SMEs are beginning to move to the industrial sectors (Sim and Pandian, 2003; Bakiewicz, 2005; Saini and Budhwar, 2008, Thai and Chong, 2008; Chelliah, Sulaiman, and Yusoff, 2010).

1.4. Classification of SMEs

SMEs are interpreted in various dimensions in various parts of the world depending on the user's perceptions. The World Bank defines SMEs based on a number of employees that is as “enterprises that employ 5 to 199 full-time employees”. On the other hand, European Commission (EC) classifies SMEs into three categories which are micro, small and medium enterprises based on the number of employees and turnover. The US categorizes SMEs based on annual turnover and export potencies. For micro-enterprises, the limit of turnover is not applicable. Meanwhile, for small and medium enterprises, the limit of annual turnover is set less or equal to US\$7 and 25 million, respectively (US Trade International Commision, 2010).

In the United Kingdom (UK), the approach used to define SMEs is almost similar to the one practiced in the US. The emphasis is given both on quantitative as well as qualitative on the features of the enterprises. Bolton Committee (BC) of UK

categorizes SMEs as “small firm with less than 200 employees and have an annual turnover of 50,000 pounds per year”. In Australia, there is no specific definition of SMEs of the government or private sectors.

The Australian Bureau of Statistics (ABS) defines SMEs as a micro business with 0 to 4 employees, small business with 0 to 19 employees and medium-sized business with 20 to 199 employees. Further, the SMEs are divided into two types of business including farm and non-farm. The SMEs farm is measured by the value of operation from A\$22,500 to A\$400,000 while SMEs non-farm has less or equal to 200 employees (Australian Government, 2011). In Malaysia, SMEs is also getting serious attention from various stakeholders including researchers and government agencies. At least 18 ministries and more than 60 agencies in Malaysia are involved in assisting the SMEs sectors (Hashim, 2000). The Small and Medium-Sized Industry Development Corporation (SMIDEC) classifies SMEs into a small business with a paid-up capital of less than RM500,000 and employs less than 50 full-time employees, medium business with paid-up capital of RM500,000 to RM25 million and employs between 51 and 75 full-time employees. The summary of the classification is shown in Table 1.1.

Table 1.1 The SMEs Classification of Countries the World

No	Classification	Employees (person)			Turnover (million)		
		Micro	Small	Medium	Micro	Small	Medium
1	European Commision ^a	1-9	10-99	100-490	< €2	€2-€9	€10-€49
2	US Committee ^b	1-499	1-499	1-499	-	\$1-\$7	\$8-\$25
3	United Kingdom ^c	1-200	1-200	1-200	£50,000	£50,000	£50,000
4	Canada ^d	-	1-99	100-499	-	C\$1-C\$50 M	C\$1-C\$50 M
5	Australian Bureau ^e	1-4	5-19	20-199	A\$1- A\$22,500	A\$ 22,600- A\$400,000	>A\$400,000
6	Malaysia ^f	-	1 - 50	51 - 75	-	< RM 500,000	RM 500,000 - RM 25Million

Source : ^a European Commision (2008)
^b US Trade International Commission (2010)
^c Meredith and Grant (1982)
^d Canada Government (2010)
^e Australian Government vernment (2010)
^f Hashim (2000)

1.5. Definition of SMEs in Indonesia

Like many other countries, the definition of SMEs in Indonesia also varies depending on the interests of users. Sometimes it is called as weak economy entrepreneurs, micro-enterprises. In some other time, it is called as small and medium industry or domestic industries. Most of them have different perceptions and criteria in interpreting SMEs thus there should be boundaries to justify SMEs definitions from different points of view. According to Tohar (1999), SMEs are defined from different points of view as follows:

- a. based on total assets, SMEs is a small business with net worth Rp200 million excluding land and buildings.
- b. based on total sales, SMEs is a small business with total sales per year Rp1 billion.
- c. based on ownership, SMEs is a small business operates an individually in the form of legal entity and not legal entities including cooperatives.

While Adiningsih (2004) identifies six agencies which provide six different interpretations or characteristics of SMEs in Indonesia. The six agencies are:

- i- Central Bureau of Statistics Agency (BPS) defines SMEs as a small business with less of 20 workers including owner and unpaid family workers. BPS furthermore classifies SMEs based on the quantity of worker, that is (1) micro-enterprises by 1-4 workers, (2) small enterprises with 5-19 workers, (3) medium enterprises between 20-99 workers and (4) the large enterprises more than 100 workers.
- ii- Bank of Indonesia (BI) defines SMEs as companies or industries having the characteristics of capital less than Rp20 million, maximum assets of Rp600 million outside of land and building, and annual turnover is less or equal to Rp1 billion;
- iii- Ministry of Cooperatives and SMEs (MENKOP dan UKM), define SMEs using Act No. 9 1995 and Act No. 20 2008, based on net wealth, annual turnover and net annual sales;
 - a) Act No. 9 1995, defines SMEs as an enterprise with a net worth Rp50 to Rp200 million (excluding land and buildings) and an annual turnover less or equal to Rp1 billion.
 - b) Act No. 20 2008 on Micro, Small and Medium Enterprises (MSME), defines SMEs as:
 - 1) Micro Enterprises are productive enterprises owned by individuals and or individual business entities that meet the criteria as micro enterprises set forth in this Act.
 - 2) Small businesses are independent productive economic activities, which is done by an individual or business entity that is not a subsidiary or branch

of the company. They are not owned, controlled, or be a part either directly or indirectly of medium or large businesses that meet the criteria of small business as referred to in this Act.

3) Medium Enterprises are independent productive economic activities, conducted by an individual or business entity that is not a subsidiary or branch of company owned, controlled, or be a part either directly or indirectly with small business or the large enterprise with total net assets or annual sales as stipulated in this Act.

iv- Ministry of Industry (*MENPERIND*) defines SMEs as small enterprises having maximum assets of Rp600 million, excluding land and buildings and working capital less than Rp25 million;

v- Ministry of Finance (*MENKEU*) defines SMEs as enterprises having a maximum turnover of Rp600 million per year or maximum assets of Rp600 million, excluding land and buildings, consist of 1) business fields (firm, Commanditaire Vennootschap or CV, Limited Enterprises (LE), and cooperative), 2) individual (craftsmen/household industry, farmers, breeders, fishers, forest encroachers, miners, traders of goods and services).

vi- Ministry of Health (*MENKES*) defines SMEs as enterprises having a quality of standard labeling or certifying such as Counseling Certificate (CC), Domestic Brands (DB), and Foreign Brands (FB).

The summary of SMEs classification is shown in Table 1.2.

Table 1.2 SMEs's Classification in Indonesia

No	Agency	Indicator used	SMEs			
			Micro	Small	Medium	Large
1	Central Bureau of Statistics Agency (<i>BPS</i>)	Workers	1-4	5-19	20-99	Above 100
2	Bank of Indonesia (<i>BI</i>)	Capital Asset Annual turnover	< Rp20 million Rp600 million ≤ Rp1 billion			

3	Ministry of Cooperatives and SMEs (<i>MENKOP dan UKM</i>)	Asset Annual turnover	< Rp200 million ≤ Rp1 billion
4	Ministry of Industry (<i>MENPERIND</i>)	Capital Asset	< Rp25 million Rp600 million
5	Ministry of Finance (<i>MENKEU</i>)	Annual turnover	Rp600 million
6	Ministry of Health (<i>MENKES</i>)	quality of standard labeling or certifying	Counseling Certificate (CC) Domestic Brands (DB) Foreign Brands (FB)

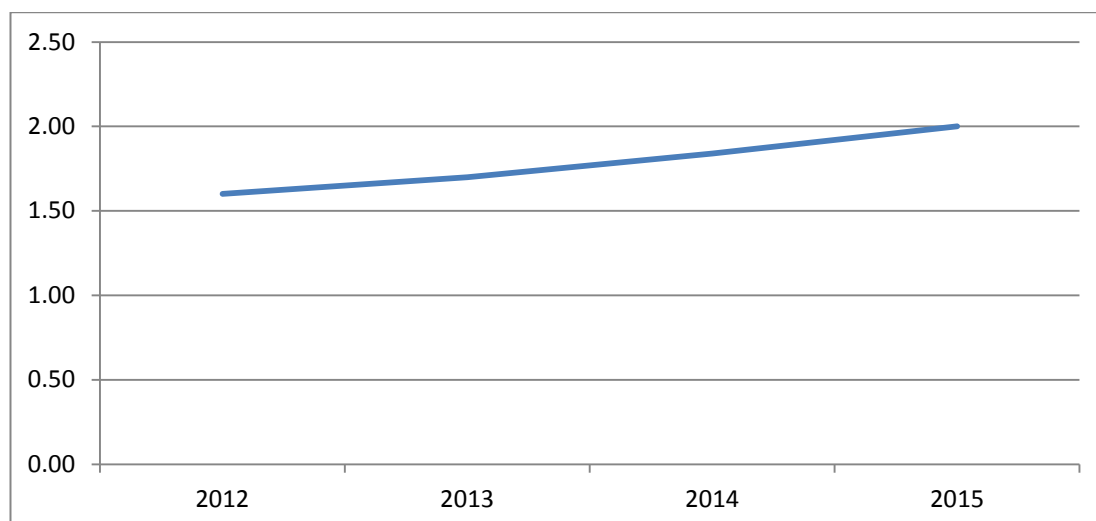
Source : Author's own compilation (2016)

SMEs interpretation by various government agencies has their own strengths and weaknesses. Bank of Indonesia use capital below Rp20 million, an asset of Rp600 million and an annual turnover of below and equal to Rp1 billion as an indicator in defining SMEs. Ministry of Cooperatives and SMEs use capital below Rp200 million and annual turnover below and equal to Rp1 billion, Ministry of Industry use capital of below Rp20 million and asset of Rp600 million and Ministry of Finance use the capital of below Rp600 million as an indicator in defining SMEs. If this definition is adopted to define SMEs in this study then most likely very few SMEs can be represented, because the SMEs in Aceh Jaya are small in nature that may not even reach Rp20 million capital. Likewise, the definition adopted by the Ministry of Health uses the certificate as labeling or branding to define SMEs. In Aceh Jaya, due to the young age of SMEs few SMEs have certificate standards as labels. Therefore definitions used by various agencies in Indonesia mainly refer to assets and turnover and may not be appropriate for SMEs in Aceh Jaya. Given that the size of SMEs in Aceh Jaya is small, the best adopted definition of SMEs for this thesis is the one as advocated by BPS. As shown in Table 1.2, BPS categorizes

SMEs into four categories. This categorization is almost similar to the one classified at the international level as summarized in Table 1.1.

1.6. SMEs Performance in Aceh Jaya

SMEs in Aceh Jaya currently plays an important role in the local economic development, it is reflected in its contribution to Gross Regional Domestic Product (GRDP) of Aceh Jaya that continuing to increase every year. Based on the survey by the Central Statistics Agency (BPS) for the past four years, the GRDP growth in Aceh Jaya is continuing to increase. In 2012 the GRDP of Aceh Jaya amounted to Rp1.60 trillion and 2013 grows amounted to Rp1.7 trillion. In 2014 the GRDP of Aceh Jaya continued to grow by Rp1.84 trillion and in 2015 reaching Rp2.00 trillion (BPS, 2016). From the statistics, the contribution of SMEs to the GRDP of Aceh Jaya recorded amounted to 44.92(%) in 2012 and increased to 45.41(%) in 2015. The summary of GRDP growth in Aceh Jaya is shown in Graph 1.1.



Graph 1.1 The GRDP growth in Aceh Jaya
Source : BPS Aceh Jaya (2016)

SMEs in Aceh Jaya operate in a wide range of economic sectors. BPS Aceh Jaya recorded that there are five sectors where the SMEs business plays an active role, among others, are sectors of agriculture, fishery, plantation, manufacturing and

culinary. In the sector of agriculture, they produce various agriculture commodity products (BPS, 2016). According to Department of Agriculture and Fishery of Aceh Jaya (2015), the SMEs business in agriculture sector produce seven types of product commodities ie paddy, chilli, peanut, corn, cassava, soybean, and sweet potato whereas the fishery produces fish products such as salted fish, anchovy, wooden fish, and shrimp. In the plantation sector, 12 main commodity products are produced namely; rubber, palm oil, coconut, coffee, areca nut, cloves, cocoa, patchouli, sago, nutmeg, kapok, and sugar palm.

Furthermore, Department of Industry, Trade, Cooperatives (2015) noted the sector of manufacturing also produced a diversity products such as products from wood materials (door frames, tables, etc), Acehese embroidery cloth, kopiah Aceh, pandan mats, beads, Acehese food and indigenous weaving whereas in culinary business as food, spices ingredient, breads, tofu and tempe, coffee, and so forth (Aceh Jaya Government, 2015).

Although SMEs contributed to regional income and involved in the various sector, SMEs is still low in productivity. The SMEs owners operate their business in household scales with the target just to fulfill the daily economic needs even though their products have a potential economic value in economic business scales.

In addition, SMEs in Aceh Jaya in general, are not yet able to utilize the local market opportunities, they lose the competitiveness from outside products. This situation causes a decline in sales volume and impact on the decrease of revenues so many of them decided to suspend their business activities. Consequently, the dependency of products on other region increases. It indicates that prices of products are sensitively influenced by goods supplies. For instance, based on the survey carried out in various traditional markets in Aceh Province published by the local

newspaper Serambi Indonesia in 2013, the prices of agricultural products changed drastically in only two weeks due to Sinabung Mountain erupted in Medan. For example, the price of onions changed drastically from Rp48,000.00 to Rp55,000.00 per kilogram in just a week. Chilies price rose from Rp28,000.00 to Rp30,000.00 per kg, and fruit prices rose 15(%) mainly for import fruits such as red wine from Rp22,000.00 to Rp80,000.00 (Bisnis, Serambi Indonesia, 28 September 2013).

The further effect is the SMEs inability in increasing the employment, even some of SMEs were forced to release their employees due to the inability in terms of equipment, marketing areas, product diversification, and wages. The next problem spread to the financial transactions disorder such as saving and loan which are stagnated subsequent to interruption of payback of capital loans from members and furthermore lead to pressures on the growth and competitiveness of SMEs.

The low productivity causing SMEs are not well organized in which the number of SMEs operates in such sectors are not recorded properly both individually and as a group. Data from both of the Department of Agriculture and Department of Plantation of Aceh Jaya are only available in the form of commodity types, the planting area, production, and average of production. However proper data for a number of SMEs involved is unavailable. According to Department of Industry, Trade, Cooperative and SMEs (2012), there were up to 265 active SMEs which produce various types of products both in goods and services which operate in sub-district in Aceh Jaya. By the end of 2013, these three departments coordinate the SMEs business actively to encourage the regional economic development.

The reviews above indicate that SMEs are facing several problems, among others, are low business productivity and profitability caused by capital shortage, improper business management and lack of skillful human resources. The difficulties

in accessing information and gaining productive resources such capital and technology causing limitations for developing SMEs. The SMEs development requires complete, quick and easy, information about potential economic sectors or commodities to be developed in a particular area. It also requires information of factors influencing its development, and prospects for the development of integrated partnership programs for the business sector or commodity.

1.7. Problem Statement

Currently, in Indonesia, the SMEs's journey are facing unfavorable situation due to differences in regulation and policies of the government which limits the SMEs movement to access resources thus unable to accommodate the beginners. To make things worse, it is also compounded by the government's inconsistency of foreign policy in SMEs development. In one point, the government protects SMEs to be able to evolve, however, on the other point, the faucet of import policy opened for goods which can be produced by the local SMEs with lower prices can trigger a fierce price competition. These situations may bring a lot of disadvantages to SMEs. The low productivity of SMEs is caused by few factors, such as awaiting the successful development of the local product through OVOP movement, few problems related to the development of SMEs products and lack of marketing strategies and support from relevant agencies to increase products value-added. In addition, the global competition is increasingly threatening where majority of SMEs in Indonesia yet to have an adequate ability in producing goods to compete in the global market and fulfill the needs of ASEAN Free Trade (AFTA), ASEAN China Free Trade Area (ACFTA) launched in 2010 and Asean Economic Community (AEC) (2015). In developing countries like Indonesia, SMEs are often linked to

coping socioeconomic problems such as poverty, unemployment, inadequate income, and gaps between rural and urban development.

Small and Medium Enterprises (SMEs) in Aceh Jaya is a priority to the regional economic development. In addition, SMEs have become the backbone of community economic system that not only aims to reduce the disparity between income groups and inter-businessman but also poverty alleviate and unemployment. SMEs development is expected to economics base and contributes significantly to accelerating its structural development, namely improving the regional economy and national economic resilience. SMEs with a good performance will be able to maintain business continuity facing the environment changing of business fast-paced. Realizing the importance of SMEs to the local economic development, it is then important to study the SMEs performance.

Performance is an important factor in SMEs business activities. The performance of SMEs is directly related to the business continuity. A good performance, despite boosting firm productivity, also plays an important role in winning the market competition either in the local and global markets. SMEs performance is also related to the individual or the owner who runs the daily operations of the SMEs. While SIV has been widely adopted, it has not been applied in Indonesia let yet Aceh Jaya. This study narrows the methodology and knowledge gap by applying SIV in Aceh Jaya to measure SMEs performance.

SMEs that are able to maintain business activities will give positive impact to community income outsourcing especially to SMEs entrepreneurs in enlarging their SMEs businesses. The growth of SMEs in the midst of communities will encourage the economic movement to continue to grow and increase and in turn, increasing the community income besides of absorbing workers broadly.

In order to maintain the existence of businesses continuity, SMEs should be able to improve their performance or at least maintain the current good performances, if any. By having good performance, the business continuity will be longer and sustained. The more the SMEs survives in an economy, the more positive impacts they would generate on income and community development. Realizing the importance of SMEs to community economic development, research on how the performance of SMEs in Aceh Jaya is and what factors influence the performance of SMEs in Aceh Jaya needs to be carried out. This study identifies factors influence the SMEs performance in terms of the characteristics of SMEs owner and the characteristics of SMEs itself.

Any level of SMEs performance plays a significant role not only in the sustainability of the SMEs but also the future direction of economic activity in Aceh Jaya. Consequently, Aceh Jaya's peoples also need to increase their SMEs performance for their continuation.

Therefore, we are interested in doing a research to measure the performance of SMEs in Aceh Jaya and what factors influencing the performance of SMEs in Aceh Jaya. Aceh Jaya is selected as research location due to the fact the government has launched an aggressive economic development program based on community empowerment. In addition, Aceh Jaya is also one of the new districts in Aceh Province. The study is expected to provide a significant information for stakeholders including the government especially in developing the SMEs business in Aceh Jaya.

1.8. Research Question

The study aims to answer the following research questions

1. How is the performance of SMEs in Aceh Jaya?.
2. To what extend do SMEs owner's characteristics (age, gender, marital status, education, business nature, occupation, experience, technical skills, family dependent) affect SMEs performance in Aceh Jaya?.
3. To what extend do SMEs characteristics (age, business license, business status, business field, number of employees, business scale, capital source, profit use, technology use, raw material source, marketing area, assistance, assistance source, type of assistance) affect SMEs performance in Aceh Jaya?.
4. What are the structural factors among the SMEs owner's characteristics and SMEs characteristics that affect SMEs performance in Aceh Jaya?.

1.9. Objectives of the Study

The main objective of this study is to examine the overall performance of Small and Medium Enterprises in Aceh Jaya, Aceh, Indonesia.

The specific objectives are:

1. To measure the performance of SMEs in Aceh Jaya.
2. To assess the SMEs owner's characteristics (age, gender, marital status, education, business nature, occupation, experience, technical skills, family dependent) that affect SMEs performance in Aceh Jaya.
3. To assess the SMEs characteristics (age, business license, business status, business field, number of employees, business scale, capital source, profit use, technology use, raw material source, marketing area, assistance, assistance source, type of assistance) that affect SMEs performance in Aceh Jaya..

4. To examine the structural factors among the SMEs owner's characteristics and SMEs characteristics that affect SMEs performance in Aceh Jaya that affect SMEs performance.

1.10 Significance of the Study

This research gives a significant contribution to the existing body of knowledge, particularly to the one applied in Aceh Jaya. Instead of focusing on the capital, this study is conducted using financial and non-financial measurement at once by expanding the factors of coverage of SMEs performance of the non-financial aspects. The initiatives are developed out in this study in order to sustain SMEs continuity while developing advanced SMEs. Further, this research is designed and developed through cross-sectional surveys with questionnaires to the SMEs owners. The findings and recommendations of this study are expected to be useful as:

- 1) contribution to knowledge on the application of SIV in measuring the performance of SMEs in Aceh Jaya. SIV as a measure of performance has never been done in Aceh Jaya. This study provides important elements and alternatives in measuring SMEs performance in Aceh Jaya.
- 2) valuable information for the government and other stakeholders about SMEs performance and influencing factors in Aceh Jaya. When the performance of SMEs increases it will positively affect the source of income, employment absorption and furthermore improving the community welfare. Therefore the government needs to get information about the performance of SMEs and the factors that affect its performance.
- 3) valuable information for SMEs owners, generally in terms of SMEs performance measurement and the influencing factors. By analyzing the information of SMEs performance, the owners of SMEs will be able to make important decisions in

developing their business including investment decisions. If the performance of the business decreases, the owner of SMEs will be able to detect the influencing factors thus proceed with anticipatory measures for the sustainability of the business.

- 4) as a guidance to further enhancing policy and decision making for the sustainability of SMEs. The results of the study can be a basic information for further analysis on the performance of SMEs so as to further enrich useful information for the interested parties.

1.11 Scope of the Study

This study is focused on the measurement of SMEs performance in Aceh Jaya using survival index value model of Abouzeedan and Busler (2004). Factors analyzed include the characteristics of SMEs owner and the characteristics of SMEs related to the performance of SMEs. Characteristics of SMEs owner consists of age, gender, marital status, education, business nature, occupation, experience, technical skills, family members. Whereas characteristics of SMEs including firm age, business license, business status, business field, number of employees, business scale, capital source, profit use, the technology used, raw material sources, marketing area, assistance, assistance source and type of assistance. Respondents involved in this study are SMEs owners where they were asked to complete a questionnaire prepared. The scope of this study addressed to SMEs in Aceh Jaya.

Respondents involved in this study were SMEs owners in Aceh Jaya where they were asked to complete a questionnaire prepared. The SMEs were those listed by the Department of Industry and Cooperative of Aceh Jaya. A number of 265 units SMEs were used as the population in the study. No sampling was done.

1.12 Organisation of the Study

The study is divided into several subsections organized as follows:

Chapter 1 describes the background of the study, SMEs development in the world and in Indonesia, problem statement, research question, objectives of the study, significance of the study and organization of the study.

Chapter 2 explains the development of SMEs in Aceh Jaya, the local government policy and indicators of SMEs performance used, and the geography of Aceh Jaya.

Chapter 3 discusses the relevant literature sources to support theoretical and empirical models, the definition of SMEs performance, types of measurement performance of SMEs, types of measurements developed, the missing gaps in the previous studies and significance of the present study.

Chapter 4 discusses method adopted and how this research will be conducted, research design, the population of study, questionnaire, pilot test, data analysis method, conceptual framework, measurement of variables, estimating factors influencing performance.

Chapter 5 presents the result analysis of factors influencing SMEs performance including descriptive analysis, SMEs performance measurement, the relationship between SMEs owners characteristic, SMEs characteristics on SME performance, ordered-logistic analysis, SEM analysis, and discussion.

Chapter 6 conclusion, presents the conclusion of the study, limitations of the study, policy implication, and recommendations.

CHAPTER 2
SMALL AND MEDIUM ENTERPRISES (SMEs)
IN INDONESIA

2.1. Introduction

The chapter gives a brief overview of the understanding of SMEs in Indonesia and SMEs performance which has commonly assessed from available sources. The chapter has four sub-sections which are OVOP as a SMEs model in Aceh Jaya, the SMEs performance, the geography of Aceh Jaya and SMEs in Aceh Jaya.

2.2. SMEs development in Indonesia

SMEs's as practiced in developed countries mainly focus on manufacturing, retail and construction activities with some adoption of innovation strategies. The specific innovation strategy will lead to the success of the business activities (Pitt and Clarke, 1999). One of the strategies which were introduced to improve the performance of the SMEs activities is the implementation of One Village One Product (OVOP). This program was firstly introduced in 1976 in Oita Prefecture, Japan, as a unique model of regional revitalization policy under the leadership of Governor Hiramatsu. OVOP has succeeded in solving social and economic disparities between villages and cities. The program emphasizes a selection of the possible product or typical industry to be fostered and marketed to the national and global level.

The basic principle of OVOP puts strong emphasis on three points; a) Local yet global; creating globally accepted products that reflect pride in the local culture, b) Self-reliance and creativity; realization of OVOP through independent actions utilizing potential of the region, c) Human resource development; fostering people

with a challenging and creative spirit (Oita Committee, 2000). Since 2006, OVOP began to be researched and adopted in many countries, particularly in Asia. The success of OVOP is already proven to improve the business productivity and competitiveness of a nation (Igusa, 2006).

In Indonesia, OVOP has been implemented in almost the same manner as that in Japan, Thailand, and Malaysia. OVOP is performed through the concept of the regional program, both at the village and district or city level. In order to protect the existence and continuity of SMEs, few policies and regulations were established by the government of Indonesia as summarized in Table 2.1.

Table 2.1 Summary Regulations on SMEs in Indonesia

NO	Year	Type of regulation	About
1	1995	Act No. 9	Small business
2	1997	Government Regulation No. 44	The partnership
3	1998	Government Regulation No. 32	The development of small business;
4	1999	President Instruction No. 10	The empowerment of medium enterprises;
5	2001	President Decree No. 127	Type business reserved for small business and medium or large enterprises with partnership pattern
6	2002	President Decree No. 56	Loan restructuring for small and medium enterprises
7	2007	Ministry regulation No. Per-05/MBU/2007	Partnership program of the state-owned enterprises to the small business community development
8	2008	Act No. 20	Micro, small and medium enterprises

Source: Adiningsih (2004)

In the period of 1998-2007, the Indonesian government has aggressively formulated the legislation to strengthen the SMEs. For example, the government issued the Decree (Keppres RI No 99, 1998) stated that SMEs need to be protected to prevent them from unfair business competitions. A policy was also embedded in the

National Long-Term Development Plan (RPJPN) 2005-2025. In 2007, the government issued the Presidential Instruction (Inpres No. 6, 2007) about the acceleration of real sector development including micro, small and medium enterprises that should be oriented on domestic products. Specifically, the government through the Ministry of Industry issued regulation No.78/M-Ind/Per/9/2007 to encourage productivity of SMEs local products to be able to compete in the local and global markets. Thus, the development of SMEs should be performed through the OVOP approach.

The OVOP approach is applied for developing SMEs based on resources and local wisdom with high added value. It is confirmed in the regulation of the Ministry of Industry No.78/M-Ind/Per/9/2007 that the development of SMEs needs to be applied through the OVOP approach to encourage competition of local products in the regional and global markets. The OVOP product is selected based on creativity of uniqueness from community businesses in villages. Products that are parts of OVOP are not only in the form of tangible products but also in the form of intangible products such as local culture and arts that increase sales value.

Since the first implementation done the Ministry of Industry, the ministry of agriculture, the Ministry of cooperative and SMEs, the government has succeeded to revitalize diverse potential products in various areas to be developed through small and medium industries (SMIs) with product-based creative. The area which participates in OVOP program (Gema Industri Kecil, 2008) shown in the following Table 2.2.

Table 2.2 OVOP Products in Indonesia

No	Regions		OVOP product
1	Jawa	- Purwakarta, Bantul and Tabanan - Tasikmalaya and Kulonprogo - Pekalongan - Boyolali - Bangil - Cianjur	Pottery / Ceramic decorative Webbing Woven and Woven fragrant roots Crafts copper Woven bamboo Silk
2	Kalimantan	Sambas and Sintang	Woven
3	Sulawesi	- Donggala - Palopo	Onions fried aromatic Palopo of chocolate
4	Sumatera	- Lampung - Tanggamus	Woven cloth from Inuh Tanggamus coffee
5	Lombok	- West Lombok - Central Lombok	Pottery / Ceramic decorative Wicker
6	Bali	- Badung	Asparagus

Source : *Gema Industri Kecil* (2008)

Note: SMEs products from Aceh Jaya have not been registered in the Ministry of Cooperative and SMEs Indonesia as the local flagship products and therefore not included in the table.

Data in Table 2.2 shows that many regions in Indonesia have potential products to be developed with high value-added value. The product of the region has been registered as the regional flagship products in the Ministry of Cooperative and SMEs Indonesia.

These products are commonly generated by SMEs business groups in limited business scale. If those can be developed properly, it will boost economic growth and income, especially for small businesses such as SMEs. The more SMEs growth, the more new job opportunities created thereby increasing the community welfare. In addition to job opportunities, SMEs product development can be also promotion tourism event of the region.

2.3. The Performance of SMEs

BPS (2016) suggested that SMEs performance in Indonesia can be viewed from several aspects, among others (1) the number of unit business and workers, (2) added value, and (3) value of export. These aspects were described in the following:

2.3.1. Business Units and Workers

SMEs in Indonesia have a significant contribution in tackling the domestic socio-economic problems mainly in terms of job opportunities and national economic growth. Most surveys conducted by experts and various institutions proved that SMEs dominantly create new job opportunities. A survey by Dipta (2005) mentioned that more than 41 million units or 99.99(%) of the total business are the SMEs and more than 76 million people or 99.4(%) are the local workforces.

Another survey conducted by Hongkong and Shanghai Banking Corporation (HSBC) in 2007 revealed that Indonesian SMEs are very optimistic to be developed. There are approximately 64(%) of business units that desire to increase business development and about 44(%) of business units have investment plans through worker recruitment (Rahmana, 2009). This survey was conducted in the period of 2005 to 2008 (<http://www.depkop.go.id>). Meanwhile, the Ministry of Cooperatives and SMEs recorded that in 2010 the number of SMEs growth was higher than the large enterprises based on the number of business units and workers as shown in Table 2.3:

Table 2.3 The Comparison Between SMEs and Large Enterprises in Indonesia

No	Business group	Unit	Workers
1	SMEs	53,823,732	99,401,775
2	Large Enterprises	4,838	2,839,711

Source: *Kementerian Koperasi dan UKM (2011)*

Data in Table 2.3 shows that SMEs are more dominant in numbers and workers compared to large enterprises. The number of SMEs reached 53,823,732 or 99.99(%) with worker employed were about 99,401,775 workforces or 97.22(%). Large enterprises, on the other hand, have only 4,838 units of enterprises or 0.0089 (%) with the amount of worker 2,839,711 or 2.77(%). In addition, the SMEs growth and

worker recruitment from year to year have also shown an increase. Data from the Ministry of Cooperative and SMEs for the period 2006 to 2010 is shown in Table 2.4.

Table 2.4 The Growth of SMEs and Workers in the Period 2006-2010

No	Description	Year				
		2006	2007	2008	2009	2010
1	SMEs units	49,021,803	50,145,800	51,409,612	52,764,603	53,823,732
2	Workers	87,909,598	90,491,930	94,024,278	96,211,332	99,401,775

Source: *Kementerian Koperasi dan UKM (2011)*

Table 2.4 indicates that SMEs has increased in numbers and worker recruitment. The number of SMEs unit in the period of 2006 to 2010 increased about 9.80(%) or 49,021,803 to 53,823,732 units while the numbers of workers employed in the same period are also increased about 13.07(%) or Rp87.9 million to Rp99.4 million.

2.3.2 Value-Added

SMEs in Indonesia play an important role in the national economic growth, as a source of the national GDP and employment. A survey by the Central Bureau Statistics of Indonesia (*BPS*) in 2009 shows that the percentage composition of Indonesia's Gross Domestic Product (GDP) derived from SMEs was 56.23(%) or Rp1,783.40 million in 2006 and increased constantly to 57.12(%) or Rp3,466.30 million in 2009.

Table 2.5 SMEs contribution to GDP in the Period 2006-2009

No	Description	Year				
		2006	2007	2008	2009	2009
1	Percentage of GDP (%)	56.23	56.28	55.56	56.63	57.12
2	SMEs contribution to GDP (million rupiah)	1,783.40	2,107.80	2,609.40	2,993.10	3,466.30

Source: *BPS (2009)*