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## **Barriers and Opportunities for MSME Development in Indonesia: Internal and External Perspectives**

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### **Abstract**

Micro, Small and Medium Enterprises (MSMEs) have a strategic role in the Indonesian economy, contributing to GDP, creating jobs and reducing poverty. However, MSMEs in Indonesia face various challenges that hinder their development, such as limited managerial skills, lack of product innovation, and limited access to financing. This research aims to identify internal and external factors that influence the development of MSMEs in Indonesia and provide recommendations to support their growth. The approach used in this research is descriptive qualitative, with data collection methods through in-depth interviews, focus group discussions (FGD), and document studies in several large cities such as Jakarta, Bandung, Yogyakarta, and Surabaya. The research results show that the main internal factors hindering the development of MSMEs are a lack of managerial skills and product innovation. Meanwhile, external factors include limited access to financing and uneven government policies. Technology and digitalization provide excellent opportunities for MSMEs to increase their competitiveness, but limited digital skills remain an obstacle. In conclusion, managerial training, product innovation, and simplifying access to financing are necessary to encourage the growth of MSMEs. The government must also improve its socialization policy and ensure its implementation is evenly distributed throughout Indonesia.

**Keywords:** MSMEs, managerial skills, product innovation, financing, digitalization

### **Introduction**

Micro, Small and Medium Enterprises (MSMEs) play a vital role in the Indonesian economy; this sector is not only the backbone of the national economy but also makes a significant contribution to providing jobs, equalizing income and reducing poverty (Hasbiah et al., 2024). Based on data released by the Central Statistics Agency (BPS), the MSME sector absorbs more than 60% of Indonesia's Gross Domestic Product (GDP) and more than 97% of the workforce; these figures show how significant the role of MSMEs is in supporting the

country's economy, especially in creating jobs and improving people's welfare (Suhaili & Sugiharsono, 2019). Therefore, it is important to continue to encourage the development of this sector so that it can contribute further to increasing Indonesia's competitiveness on the global stage (Susanti et al., 2023).

Despite having a significant contribution, MSMEs in Indonesia face various challenges in their development process; one of the main challenges MSME players face is limiting access to capital (Shahrullah et al., 2021). Many micro and small business actors have difficulty obtaining sufficient financing to develop their businesses, both from formal and alternative financial institutions; apart from that, the problem of lack of adequate managerial skills is also an obstacle in business management (Tambunan, 2011). MSME players are often hampered in planning strategies, managing human resources and efficient financial management (Berliana & Habibburrahman, 2024). Tight market competition from fellow MSMEs and large companies also adds to the difficulty for them to survive and develop; this makes the MSME sector in Indonesia face significant challenges in optimizing existing potential (Salsabila et al., 2024).

This research aims to dig deeper into the various factors that influence the development of MSMEs in Indonesia, both internally and externally. Internal factors such as managerial skills, human resources (HR) quality, and product innovation capabilities are important keys to developing MSMEs. Apart from that, external factors also play a significant role, such as government policies that support the growth of MSMEs, easier access to financing, and adequate infrastructure development. Several government policies, such as microfinancing programs and entrepreneurship training, have indeed been implemented, but their implementation still needs to be improved so that more MSMEs can feel the benefits. By understanding these factors, it is hoped that the MSME sector can develop more optimally and significantly contribute to the Indonesian economy.

MSMEs also play an important role in equalizing income in Indonesia; by spreading businesses more evenly across various regions, both in cities and rural areas, MSMEs can reduce existing economic inequality (Remmang et al., 2023). Apart from that, MSMEs can survive and adapt amid the global economic crisis; this ability to survive makes MSMEs an important pillar in the Indonesian economy, which can provide stability in facing various global economic pressures (Dewi et al., 2023). Furthermore, the role of MSMEs will be increasingly strategic in the digital economic transformation process; as technology continues to develop, MSMEs have the opportunity to expand their markets through digital platforms, reach wider customers and increase operational efficiency (Hariyanti & Kristanti, 2024).

Digital technology development also challenges MSMEs in Indonesia; even though technology provides excellent product marketing and distribution opportunities, many MSMEs have difficulty adapting to these changes (Hendrawan et al., 2024). Most MSMEs are still accustomed to traditional ways of running their businesses, so they are hampered in making maximum use of digital technology; in fact, technology can increase the competitiveness of MSMEs, expand market reach, and simplify the product distribution process (Ningsih & Tjahjono, 2024). For example, using an e-commerce platform can help MSMEs sell their products to consumers throughout Indonesia and even internationally (Achmad, 2023).

## ***Barriers and Opportunities for MSME Development in Indonesia: Internal and External Perspectives***

Therefore, MSME players need to improve their technical capabilities in managing their business digitally to take advantage of existing opportunities and remain relevant in the digital era (Mesakh, 2024).

### **Literature Review**

According to Law of the Republic of Indonesia no. 28 of 2008 in Indonesia, MSMEs (Micro, Small and Medium Enterprises) are a category of business which is differentiated based on the scale or size of the business, which is determined by specific criteria such as annual turnover, number of assets and number of employees. According to Law of the Republic of Indonesia no. 28 of 2008 in Indonesia, MSMEs are divided into three main groups, namely micro, small and medium enterprises. Micro businesses are businesses that have a maximum annual turnover of IDR 300 million and fixed assets of a maximum of IDR 50 million. Usually, micro businesses are run by individuals or small families with a small workforce and are often informal. Small businesses have an annual turnover of between IDR 300 million and IDR 2.5 billion, with fixed assets ranging from IDR 50 million to IDR 500 million, and tend to have more workers than micro businesses. Meanwhile, medium businesses have an annual turnover of between IDR 2.5 billion and IDR 50 billion and fixed assets of between IDR 500 million and IDR 10 billion, with more extensive and professional operations than micro and small businesses.

MSMEs contribute considerably to the Indonesian economy because they provide jobs for the community and contribute a significant proportion of the gross domestic product (GDP) (Hasibuan et al., 2024). The Indonesian government recognizes the importance of this sector, so it provides various programs and policies to support its growth, such as providing access to capital, skills training, and ease in marketing products (Adam & Negara, 2015). With rapid growth and proper support, MSMEs in Indonesia are expected to become the main pillars in creating prosperity and reducing economic disparities while strengthening global competitiveness (Salsabillah et al., 2023).

### **Research Method**

This research uses a qualitative approach to explore the factors influencing the development of Micro, Small and Medium Enterprises (MSMEs) in Indonesia. This approach was chosen because it aims to understand the perspectives of MSME players and related stakeholders regarding the challenges and opportunities they face in developing their businesses. With a qualitative approach, researchers can gain more complex insights into aspects that cannot be explained through numbers or statistics alone. The type of research used is qualitative descriptive research, which aims to describe in detail the internal and external factors that influence the development of MSMEs and the challenges and opportunities faced by MSME actors.

This research will be carried out in several large cities in Indonesia, such as Jakarta, Bandung, Yogyakarta and Surabaya, which were chosen because they have a high concentration of MSMEs. Research subjects include MSME actors from various sectors and related stakeholders, such as financing institutions and the government. Data collection techniques include in-depth interviews, focus group discussions (FGD), and document study. In-depth interviews were conducted with MSME actors and related parties to explore their experiences, while FGDs were conducted to obtain broader views from several MSME actors in one group. Document studies were carried out to analyze government policies and data related to MSMEs, which can provide a broader context for this research.

## **Result and Discussion**

Based on in-depth interviews, focus group discussions (FGD), and document studies conducted in this research, several internal and external factors influence the development of Micro, Small and Medium Enterprises (MSMEs) in Indonesia.

### **Internal Factors**

One of the internal factors often highlighted in the management of MSMEs is the limited managerial skills possessed by business actors. Many admit that despite having technical expertise in their field, such as production or service, they often lack crucial managerial aspects. Skills in financial planning, effective marketing, and human resource management are often lacking, thus hampering their business development potential. The results of interviews with MSME players in various big cities such as Jakarta, Bandung, and Yogyakarta revealed that less-than-optimal business management is often the main obstacle to increasing the scale and competitiveness of their business. Many MSME players find it challenging to prepare a thorough business plan, manage the budget efficiently, or develop the right marketing strategy to reach a broader market. Even though they have good products, ignorance in planning and managing finances and the inability to manage human resources often prevent their businesses from developing and competing with larger companies.

One of the other significant challenges MSME players face is the lack of innovation in their products. In an increasingly competitive market, MSMEs often find it difficult to differentiate their products from similar competitors' products. Several business actors stated that their products tend to have characteristics and qualities almost the same as products already on the market, so they do not have advantages that are attractive enough for consumers. This leads to limitations in creating a strong appeal in the eyes of consumers, which ultimately results in sales stagnation and difficulty in expanding market share. That is, the gesture to innovate not only limits the appeal of their products but also limits long-term growth potential. Without continuous product development, MSME players will find it difficult to survive amidst rapid changes in market trends. Finally, innovation in products and business processes is significant in maintaining relevance in the market and increasing the competitiveness of MSMEs.

## ***Barriers and Opportunities for MSME Development in Indonesia: Internal and External Perspectives***

### **External Factors**

From an external perspective, one of the main problems hindering MSMEs is limited access to financing. Even though the government and financial institutions have provided various financing programs to support the development of MSMEs, many business actors have difficulty accessing these funds. One of the main obstacles is their inability to fulfil set requirements, such as having collateral or adequately maintained financial records. Many MSMEs, especially those who are just starting or have been operating in the informal sector, do not have access to the necessary collateral facilities or do not have neat and transparent financial records. This often hinders them from obtaining business expansion financing or overcoming working capital problems. In interviews with MSME actors in Surabaya, it was found that complicated procedures and requirements that were difficult to fulfil were the main obstacles in gaining access to the required financing. Although they have excellent business potential, there are many obstacles caused by bureaucracy around access to funds that would otherwise support their development.

Even though the government has established policies to support the MSME sector, the effectiveness of implementing these policies is still often considered less than optimal. Some MSME actors, especially those in remote areas or with limited access to information, feel that existing policies have not fully reached them. Many MSME players complain about the lack of socialization regarding government policies or programs that should be able to help them, such as interest subsidies or business training. As a result, they cannot take advantage of the available help or support. For MSMEs in more protected areas, access to these facilities is more limited due to the lack of adequate infrastructure and resources to access information or participate in the programs offered. The inequality in the distribution of these policies hampers the ability of MSMEs to compete in an increasingly competitive market. In other words, even though existing policies are designed to help, their uneven implementation causes many MSME players to feel left behind and find it difficult to develop further.

### **The Influence of Technology and Digitalization**

One of the important findings in this research is the significant role of technology and digitalization in increasing the competitiveness of MSMEs. The many MSME players who have adopted digital platforms for product marketing and distribution show they can reach a broader market and increase their sales volume. By utilizing social media, e-commerce and other digital applications, they can introduce their products to consumers who were previously difficult to reach. This digitalization process also allows MSMEs to optimize their operations, speed up transactions and increase efficiency. In addition, with digitalization, businesses can access more relevant market data, which helps them understand consumer needs and respond quickly.

Many MSME players are aware of the great benefits of technology; the main obstacle they face is a lack of skills in using digital technology. Based on the results of the Focus Group Discussion (FGD) conducted in Yogyakarta, most MSME players admitted that they had difficulty adapting to new technology, especially regarding online marketing and digital payment systems. This creates a gap between those who have adopted technology and those

who still rely on traditional marketing methods. Therefore, there is an urgent need to increase training in the field of digitalization so that MSMEs can optimize the potential of technology. This training should cover fundamental aspects of using digital technology and ways to manage online marketing and transactions more effectively.

### **Infrastructure and Market Access**

Infrastructure factors also play an important role in the development of MSMEs. Based on interviews with MSMEs in Bandung and Surabaya, limited access to adequate infrastructure is often the main obstacle in their business operations. One of the main issues often complained about is the poor condition of roads and transportation, which hinders product distribution, especially in more remote areas. Slow internet access is also a significant problem because many MSMEs rely on internet connections to run their business for marketing, transactions, and communication with consumers and suppliers. Without sound and stable access, they are hampered in innovation and achieving wider market opportunities.

Apart from that, there is the problem of inefficient distribution of goods and welfare conditions. Several MSME players revealed difficulty sending products on time, especially to areas further from the city centre. This condition affects customer satisfaction and reduces consumer confidence in their products. Therefore, improving physical infrastructure, such as roads and transportation facilities, and digital infrastructure, such as fast and stable internet connections, is necessary to support the development of MSMEs. These improvements, especially in more remote areas, will be critical in increasing the competitiveness of MSMEs locally and globally, enabling them to grow more rapidly in an increasingly competitive market.

### **Conclusion**

MSMEs have a vital role in the Indonesian economy, significantly contributing to GDP and employment and reducing poverty. However, the development of the MSME sector still faces several internal and external challenges. From an internal perspective, limited managerial skills and lack of product innovation are the main obstacles for MSME players in optimizing their business potential. Meanwhile, from the external side, limited access to financing and uneven implementation of policies are other inhibiting factors. Even though the government has established various policies and programs to support MSMEs, many business actors still have difficulty taking advantage of these opportunities.

To support the growth of MSMEs, more systematic efforts must be made to address managerial skills and product innovation issues. More intensive managerial training and education, as well as product innovation development programs, must be introduced to increase the competitiveness of MSMEs. The government must also provide financing procedures and expand access to capital for MSMEs, especially those in the informal sector. In addition, outreach regarding existing policies and programs must be carried out, especially in remote areas, to ensure that MSMEs can utilise the available support. Lastly, more even policy

## ***Barriers and Opportunities for MSME Development in Indonesia: Internal and External Perspectives***

implementation throughout Indonesia must ensure that all MSME players can compete fairly in an increasingly competitive market.

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