

THE SOCIAL IMPACT OF MICROFINANCE INSTITUTIONS IN EMPOWERING BOTTOM OF THE PYRAMID GROUPS (BoP) The Case Study of Koperasi Kasih Indonesia

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Abstract

This article aims to analyze the social impact of Koperasi Kasih Indonesia (KKI) as a microfinance institution (MFI) in terms of the form of benefits received by its members and how to measure them. Conventionally the parameters of range expansion (outreach) in disbursing microcredit are widely used to measure the social impact of MFIs. The more extensive reach also indicates the potential benefits that can be obtained by Microfinance Institutions (MFIs). Therefore, if it is separate from the social mission of the MFI, the target reach will only encourage the commercial motive of the MFI. On the other hand, measuring the social impact of MFIs takes work and requires more funding. This paper is a descriptive case study of Koperasi Kasih Indonesia (KKI) that aims to identify the social impact of KKI on its members by using Social Impact Causal Chain model. The results found that there are two types of social impacts of KKI, quantitatively and qualitatively. These two impacts also explain the transformation process of KKI members who originally received benefits from KKI more in material form (tangible) to be more immaterial benefits of KKI (intangible). The research also found that there are superior KKI factors such as the commitment to the social mission of KKI which is implemented in service programs innovatively, supported by organizational governance and values instilled in KKI officers and members strongly.

Keywords: *microfinance, cooperative, social impact*

1. Introduction

One of the development issues is how to drive the economy to the bottom of the pyramid (BoP). The BoP group is those with an income of < US\$2 per day (Prahalad, 2004). Globally, about 4

billion people, or half the world's population, live on less than US\$2 a day, and that figure is growing at 8% a year. They have no access to and are excluded from the formal market.

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For so long, the economy at the bottom of the pyramid was seen as a problem than a potential. The informal sector is often regarded as illegal, unproductive, and unregulated, even though they constitute the majority of the business sector in Indonesia. Prahalad (2004) showed the potential and benefits that can be obtained with the business of BoP community groups which then inspired social enterprises and corporations engaged in the BoP sector, and various business models succeeded in raising the standard of living of those in BoP.

Micro enterprises are often called with the term of “economically active poor”, the business sector with the largest number of business units and labor, weak in legality and access to financing, so it takes work to develop. Financing is a decisive factor for micro businesses to grow. The problem of "unbankable" causes micro-enterprises to fall on the loan shark system for financing.

Microfinance is a financial service mechanism for the poor who develop productive businesses using

unconventional mechanisms and procedures. In developing countries, the poor have to seek informal loans to meet their household and business expenses, with high-interest rates from loan sharks. This informal debt further marginalizes them and leads them into a deeper cycle of debt and poverty.

Koperasi Kasih Indonesia (KKI) is a microfinance institution (MFI) that applies the Grameen model. Most KKI members have an income of US \$ 2 – 5 (or Rp 30,000 – 100,000) daily. The cooperative that serves financing for lower community groups and micro enterprises in Cilincing, North Jakarta was established in February 2011 with an initial number of 24 members. The funds channelled for the loan came from the personal funds of the founders and donors. Eight years later, KKI has succeeded in disbursing loans reaching Rp 13 billion, with an active membership of 9,892 people and six branch offices.

Currently, microcredit is a promising portfolio for banks in Indonesia. The number of micro business loans continues to increase.

Outstanding microloans in April 2019 were IDR 263.914 trillion and doubled in December 2022 to IDR 532.724 trillion (Source: Indonesian Economic and Financial Statistics, Bank Indonesia 2019 and 2022). Another fact that explains the microfinance market is still promising is the low number of banking customers, where the number of new bank account owners reached 80.27 million people or 40.3% of the total population of Indonesia (2020). This means that banking services have not reached the majority of Indonesia's population and are a large market for microfinance. Business era fintech (financial technology peer-to-peer lending) also changed the landscape of microfinance business in Indonesia, where the amount of funds disbursed continued to increase. At the end of 2022, loan accumulation Fintech reached Rp 601.41 trillion. With a growing number of micro business loans, assessing the impact is important, but there is a research gap in this area.

The research was conducted to see the performance of KKI as an MFI in creating social impact for its members

or representatives and maintaining the sustainability of KKI institutions on an ongoing basis amid challenges and problems. What are the social performance indicators of KKI, and what factors influence it?

2. Literature Review

2.1 Micro Finance

Microfinance is a method of financing for poor groups carried out by adequate collateral replacement for the working capital of beneficiary clients and is short-term (CGAP - Consultative Group to Assist the Poor, 2005). The World Bank defines microcredit as a process in which a poor family borrows a sum of money and pays the amount in small repayment instalments that can be managed over a realistic period using social security in the short or long term (Christopher and Gilbert, 2017).

Compared to traditional loans, microcredit has more specific characteristics. Loans from microcredit programs are usually small amounts and have shorter repayment cycles. Christopher and Gilbert (2017), referencing Du (2004), argue that the

main difference between microcredit and conventional lending is that it targets borrowers from poor and low-income groups. Microcredit emphasizes lending to poor women disproportionately represented among the world's poorest people. The absence of collateral makes microcredit services rely on borrower discipline through group mechanisms, namely reciprocal accountability mechanisms (Christopher & Gilbert, 2017).

Microcredit Summit 1997 formulated that microcredit programs should provide small loans to poor people for entrepreneurial activities and enable them to support their families. Several aspects are generally agreed upon as microfinance: reaching out and empowering the poor, and developing sustainable institutions

2.2 Social Performance Indicators as the Main Aspects of MFIs

Microfinance was born due to conventional financial institutions failing to fight poverty. To its mission, MFIs are committed to reaching the

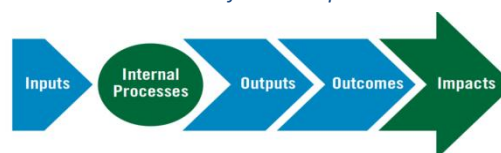
poor, but sometimes many face tensions between the choice of earning income and expanding social impact (Mia & Chandran, 2016). The complexity in measuring social impacts is faced by MFIs considering that there are many parties (investors, shareholders, etc.) with different interests in looking at the performance of MFIs (Beisland et al., 2020) while assessing the social impact of MFIs requires a lot of funds (Dacanay, 2009).

Hence the range of microfinance services (outreach) became a widely used leading indicator to measure the social impact of microfinance (Dacanay, 2009; Thrikawala et al., 2013). The range can be distinguished into two categories: the level of depth of range (depth outreach), namely the poverty level of the clients served, and the level of breadth of reach (breadth outreach), i.e., the number of clients served. MFIs must maintain performance, both from social aspects and financial sustainability (Bibi et al., 2018; Beisland, et al., 2020).

Commercial motives encourage MFIs to target a larger number of clients and maintain their financial performance. MFIs operate as efficiently as possible. As a result, many essential aspects are omitted (Hermes et al., 2011; Nurmakhanova et al., 2015). However, financing poor loans with minimal loan amounts is unprofitable, as it is more expensive than servicing less poor clients with larger loans (Hermes et al., 2011). On the other hand, financial literacy is fundamental and needs to be a mandatory training component for microfinance programs. Socioeconomic training has a significant positive impact on the lives of female microfinance beneficiary clients and contributes to the transformation of their household and business power (Nawaz, 2015). Research by Komson, et al. (2023) shows the poverty reduction impact of financial literacy and financial inclusion activities from microfinance in Tanzania, Kenya, and Uganda. Financial literacy also affects increasing entrepreneurial abilities.

Therefore, parameters must be used to measure the performance and social impact generated by MFIs. Dacanay (2009) offers a Social Performance and Management Flow, where social impact can be described as a continuum of a chain of means and ends. Measurement of MFI social performance indicators (Social Performance Indicator, Social Performance Management) began to appear in 2002 initiated by world bodies, such as the World Bank, CGAP, CERISE (Thrikawala et al., 2013).

Chart 1 : Causal Chain of Social Impact



Source : Social Performance Progress Brief, March 2007

The Social Impact Causal Chain chart developed by SEEP Network explains as follows:

- 1) Input: Includes the intention and mission of the MFI and the design of the MFI. The main question is: What is the mission of the MFI, and are its social goals clear enough?
- 2) Internal Process: What activities will MFIs carry out to achieve their

social mission? Has the system been built to achieve these goals?

- 3) Outputs: Does the MFI serve the poor and the very poor? Are MFI service products appropriate and answer their needs?
- 4) Outcomes: Is the client progressing socially and economically?
- 5) Impacts: How far has progress been made concerning institutional activity? How have MFIs created a socio-economic transformation of society?

3. Research Methods

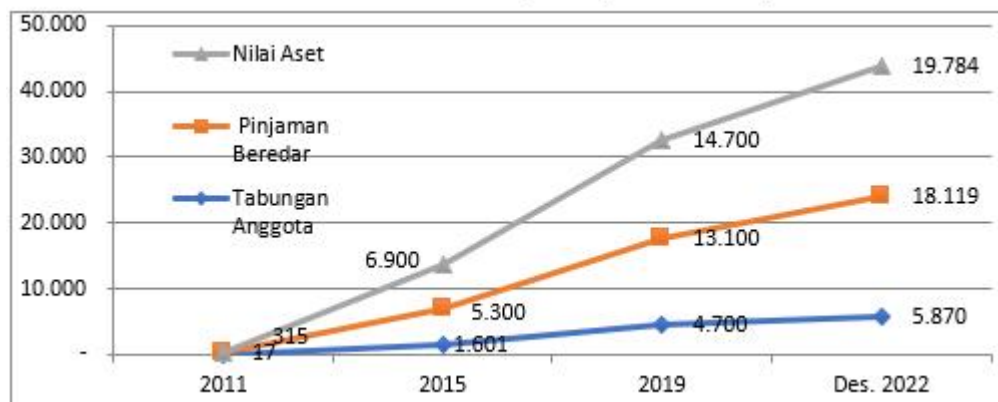
This descriptive research uses the case study method of the Koperasi Kasih Indonesia (KKI). Data is collected from various sources in the form of primary and secondary data. Primary data include interviews with KKI

administrators and supervisors, KKI members, MFI managers, and the results of focus group discussions (FGDs) with several KKI groups. Secondary data includes documentation and reports published by KKI and other sources. Data processing is carried out by classifying data according to themes and categories to describe a phenomenon and characteristics of the object of research and explain the role and interaction of individuals and social relations that occur (descriptive exploratory).

4. Discussions

4.1 KKI Performance Achievement for 10 Years

Over a period of 10 years (2011-2022), KKI has grown and experienced various achievements as can be seen in the graph below.



Grafik 1

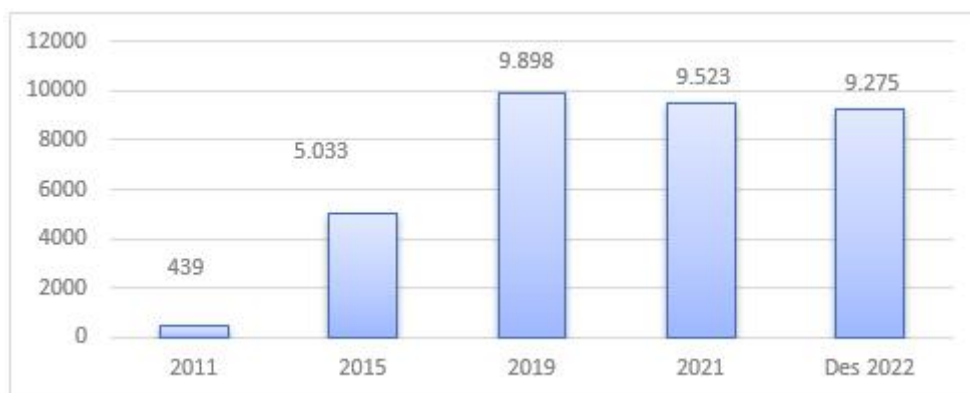
Total Outstanding Loans, Total Savings and KKI Assets In a few years (2011 - 2022)

Source: KKI Annual Report (2022)

The value of KKI's assets grew by more than 100% from 2015 to 2019. Meanwhile, funds disbursed as loans also increased sharply, from Rp 315 million in 2011, to Rp 18.12 billion (December 2022). Likewise, member savings, initially only IDR 17 million in 2011, continued to increase and reached IDR 5.87 billion (December 2022).

The above increase is also in line with the number of members, from 439

people in 2011 increasing almost 12-fold to 5,033 people in 2015. Then it increased by 80% during the period 2015 – 2019 to 9,898 people. The Covid-19 pandemic has become a tough challenge for the KKI, one of the impacts of which is the decline in the number of members from 2019 - 2022, as shown in the graph below.



Grafik 2
Number of KKI Members 2011-2022

Source: KKI Annual Report (2022)

The two graphs above (Graph 1 and Graph 2) explain the sharp increase in financial performance and the number of members in 2015 – 2019. This situation explains that the need for members for loans and interest in saving is increasing from time to time.

Initially, KKI measured social impact by measuring the improvement of the welfare of its members. In reality, some social impacts can be measured quantitatively, some are qualitative. KKI continues to improve to be able to measure this social impact better. The

following is the social impact KKI's performance has on its members.

4.2 Coverage Expansion

In the beginning, KKI believed that expanding outreach by increasing the number of clients was significant to improve performance, so this became a measure of the social impact of KKI's. This can be seen in Graph 2 above, wherein the period 2011 - 2015, there was a sharp increase in the number of members. In addition to coverage, bad loan levels are also an important performance indicator. Low bad credit indicates the member is disciplined and able to repay the loan. This provides an opportunity for KKI to disburse even more loans and reach those who need more loans. The increasing value of member loans indicates the increasing welfare condition of members, so they need a larger financing scale. However, the view of achieving targets by pursuing as many customers or clients as possible causes MFIs to compete using aggressive methods. It is no different from what financial institutions do in general. KKI then evaluates that it contradicts the mission and initial spirit of KKI standing.

Much energy is devoted to meeting the target, while KKI has another mission that must be achieved, namely member education and member savings.

4.3 Savings and Independence

Amid intense competition from MFIs for clients, the loyalty of KKI members remains high. KKI administrators and members have the same answer because KKI educates them to save. The members revealed that what they felt most about the existence of KKI, besides obtaining loans, was the benefits of saving training and education that changed their mindset and made them more independent. For KKI providing loans is a strategy as an entry point to educate members to save. KKI requires that every loan instalment is set aside for savings. When the loan is paid off, the member already has some money in his passbook, which is often only realized after. Some members said that before joining KKI, they never imagined they could save. The savings are beneficial for members for school expenses, business capital, renovating houses, opening boarding houses, and others. They then

feel more about the benefits of KKI that they can have savings rather than loans. Therefore, the level of member savings is a form of the social impact of the existence of KKI, namely the transformation process from dependence on loans to independence by saving. In 2019, the number of KKI members who saved Voluntary Savings regularly reached 42%. However, in 2020, due to the impact of the Covid-19 pandemic, the number dropped dramatically to 12.4% and began to increase again to 18.2 at the end of 2022. On the other hand, despite a decrease in the number of members saving, accumulatively, the number of members savings has increased, as shown in Table 1 below.

Table 1.
 Percentage of KKI Outstanding Loan

	2011	2015	2019	2022
Member Savings Amount	IDR 17 million	Rp 1,601 billion	Rp 4,7 billion	Rp 5,87 billion
Percentage of Member Savings against KKI Outstanding Loan	12,88%	28,09%	36,15%	32,40%

Source: KKI Annual Report (2022)

KKI's efforts to build member independence can be seen from the increase in member savings from time to time, with an increasing percentage of the credit balance (outstanding loan) during 2011 - 2019. In 2022, although members' savings increased, the percentage of credit balance decreased due to the high need for member loans during the Covid-19 pandemic (2020-2022). The group and group leader play an essential role in instilling the values of the KKI. The head of the group always encourages its members to save because they have felt the benefits of saving for the growth of their business.

4.4 Member Training and Mindset Changes

The KKI strictly requires member training. This is done from the process of receiving members to the process of providing loans on an ongoing basis. The training has opened up members' horizons. Even some members feel "KKI training is number one" compared to loan and savings services. Those with such awareness are dubbed KKI as "outliers" who have

experienced a change in mindset by attending training and experiencing a leap of progress.

KKI considers the problem of poverty more due to the mental readiness of the poor than access or opportunity. Access and opportunity could exist but cannot be utilized because they must prepare. Transforming members who originally borrowed and finally saved is a process of changing their mindset. At first, members need to be made aware of the

benefits of savings. But when the loan is paid off, he has savings. The members experienced a change in mindset, initially thinking about debt, then realizing they could save.

In business, KKI's main service product is loans. But lending is a strategy of an extensive process carried out by the KKI, to motivate and encourage the poor so that they are able to take life actions that will allow them to get out of poverty permanently, as described in Chart 2 below.



Chart 2
Three Stages of KKI Approach

Source: KKI Annual Report (2022)

From the discussion above, it can be concluded that KKI members experienced a process of changing their mindset. Who originally had a view (mindset) of needing money and wanted to join KKI because they got money loans, gradually their views changed to want to have savings and want to be independent. The confidence of

members to be independent is even greater, who initially, as individuals feel unable to control money and have no dreams or hopes become individuals who can control money and encourage their desire to move forward and confident can realize their dreams.

4.5 KKI Values and Collective Responsibility

Another benefit felt by members from the presence of KKI is related to attitudes, habits, and solidarity values. Through group mechanisms, KKI instils values in members. In the FGD, the members mentioned: discipline, thrifty, perseverance, tenacity, and solidarity together are the values they get from the KKI. Members explained the attitude of KKI officers who always keep promises, arriving on time even if it rains or floods. Strong discipline and keeping promises bond members to do the same. Group members consistently fulfil deposits on time. During depositing activities, it always begins and ends with a prayer. This is a strong impression for members always to have good intentions, not underestimate the opportunities they receive.

Another value that KKI instils in member groups is a mutual responsibility. This is introduced to members from the beginning of the training and repeatedly conveyed to members that the importance of

solidarity and togetherness of members so that there are no problems with member deposits. Members faithfully carry out their responsibilities. If members have problems that cannot be deposited because of family problems, sick children, etc., then the group is willing to bail out together.

4.6 Social Impact of KKI

From the description above, it can be concluded that despite reaching low-income groups with microcredit services, the social impact is a savings and training service that opens members' horizons and provides opportunities for them to become independent human beings.

Using the Social Impact Causal Chain model (Social Impact Causal Chain) developed by SEEP Network, the social impact of KKI can be explained as follows:

1) Internal Process :

- The three-stage KKI approach through training, microcredit loans and savings services has created a process of transforming members economically into more

prosperous and independent (Chart 2).

- The education provided to members has changed the mindset of those who were initially dependent on loans and had no future to become more independent and dare to dream.
- Group mechanisms and mutual responsibility systems become a binding rope to foster a sense of solidarity among members.

2) Outputs :

The external forms of social impacts produced by KKI are:

- Commitment to reach and serve the neediest, namely those with an income of Rp 30 – 100 thousand per day, as seen in the growth data of KKI members (Graph 2).
- The increasing number of member savings, where microcredit services and KKI savings have provided opportunities for KKI members to grow into independent human beings (as shown in Graph 1 and Table 1).

3) Outcomes :

KKI efforts have given birth to a change in mindset and independence in KKI members as well as the growth of bonds and a sense of group solidarity. Indeed, this finding is qualitative. The phenomenon of member transformation can be recognized from those who initially relied on loans turned into savings-oriented. While the members who have experienced a leap (outliers considered), the most significant benefit of KKI is the training because it has changed their mindset.

4) Impacts :

- Progress achieved related to institutional activities:** KKI has been running for more than 10 years, and their business continues to grow in terms of increasing the number of members (clients) served, the amount of credit disbursed, increasing the amount of third-party fund participation, increasing income and assets providing greater opportunities for KKI to continue to contribute to community empowerment, expanding their services and maintaining business continuity.

- ii. **The process of socio-economic transformation of the community:** There is an increase in the welfare of members in the form of the development of their businesses and the growth of independence. There was a change in the mindset of KKI members from those who previously faced debt traps, had no future, and were afraid to dream, became independent individuals who had a future and dared to dream. The independence of members also causes them to have more inertia and resilience when disasters occur, such as the Covid-19 pandemic.

This finding is in line with the results of Wangsa and Kumar's research (2021), microfinance apart from helping grassroots groups, empowerment efforts have reduced their dependency, created independence with the growth of self-help groups, and increased members' savings as a form of self-reliance for those who originally depended on loans.

5. Conclusions

Departing from the nature of microfinance to empower the bottom of the pyramid (BoP) groups, measuring the social impact of MFIs is an essential part of MFI performance. The target of expanding outreach, i.e., how much microfinance reaches the poor, is a commonly used indicator. However, there are many weaknesses of this as an indicator of the social impact of microfinance because the nature of microfinance is not enough just to reach the poor but there are aspects of literacy, empowerment, sustainability, and others.

When microfinance is only seen as a business opportunity, the range indicator will only explain the profit potential of the funds disbursed. Therefore, the motive and how the microfinance product is delivered to the client will determine the social impact of microfinance.

Intention toward social mission is the key that drives MFIs to innovate and develop strategies in responding to social problems. The social impact of KKI is a process of various interrelated aspects, namely, first, a solid commitment to help the poor and build member independence. Second, the

innovation of service products other than loans, education, and savings are interrelated with one unit.

Through Social Impact Causal Chain Model it can be explained the social impact of KKI as a performance of the input, output, outcome, and impact processes. The social appearance of KKI can be divided into quantitative and qualitative aspects. Quantitatively in the form of increasing the number of KKI members, the amount of microcredit distributed, and the number of member savings indicates members' financial independence. Qualitatively, the transformation process experienced by KKI members. The transformation process can be explained by the situation of members who initially felt the benefits of KKI in the form of providing money loans turned into knowledge, changing new mindsets and awareness. Thus, there is a change in the pattern of member relationships with KKI, which were initially clients who needed loan funds, changed to relationships that have stronger ties because of the same values. A process of transformation of relations from material ones (tangible) become immaterial (intangible). This research is qualitative and, in the future, can be

developed into quantitative research to obtain more measurable data on the social performance of MFIs.

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