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The Role of Microfinance Institutions in Supporting Financial Inclusion and Economic Empowerment in Indonesia

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A B S T R A C T

This research aims to examine the role of Microfinance Institutions (MFIs) in supporting financial inclusion and community economic empowerment, especially for the poor and micro-entrepreneurs in Indonesia. Using a normative juridical approach, this research analyzes the regulations and operations of MFIs based on Law No. 1 Year 2013 on MFIs as well as secondary data from literature and interviews with relevant practitioners. The research was conducted for three months, from June to August 2024, focusing on MFI regulations, operations, and challenges in Indonesia. Data were collected through literature study, legal document analysis, and in-depth interviews with 20 respondents located in the West Jakarta area, including MFI managers, micro business actors, and academics. The results show that MFIs play an important role in providing microfinance, savings, and business advisory services that support economic empowerment and community welfare improvement. However, regulation implementation still faces challenges, including policy harmonization between central and local governments, limited capital, and low financial literacy of customers. In addition, competition with modern financial institutions is also an obstacle to the sustainability of MFIs. This study recommends strengthening regulations, harmonizing policies, and increasing the operational capacity of MFIs through technical support, training, and capital incentives. Financial literacy also needs to be improved so that people can optimally utilize microfinance services. Thus, MFIs can be a more effective instrument in supporting sustainable economic development and financial inclusion in Indonesia.

1. INTRODUCTION

Microfinance has grown rapidly in the last two decades as one of the key strategies in reducing global poverty (Arda, 2024). Since the success of the Grameen Bank program pioneered by Muhammad Yunus (2006 Nobel Peace Prize laureate) in Bangladesh in the early 1980s, global attention to microfinance has increased significantly. Microfinance is not only considered as a solution to alleviate poverty, but also as a mechanism capable of creating sustainable economic benefits (Van et al., 2021).

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I.16. POSISI KREDIT USAHA MIKRO KECIL DAN MENENGAH BANK UMUM (UMKM) [1]

(Miliar Rp)

	KETERANGAN	2018	2019	2020	2021	2022	2023	2024	*ITEMS*
1	**UMKM**								***MSMEs***
2	**Lapangan Usaha**	**1,032,643**	**1,111,340**	**1,091,232**	**1,223,433**	**1,351,249**	**1,460,164**	**1,507,063**	***Industrial Origin***
3	Pertanian, Kehutanan dan Perikanan	101,811	118,923	141,428	176,207	230,219	262,302	280,667	*Agriculture, Forestry and Fishery*
4	Pertambangan dan Penggalian	6,696	8,248	8,019	8,893	6,969	7,831	9,427	*Mining and Quarrying*
5	Industri Pengolahan	101,845	110,661	111,752	127,292	134,879	144,551	147,969	*Manufacturing Industry*
6	Pengadaan Listrik dan Gas	4,284	6,120	3,474	3,193	3,034	3,697	3,462	*Electricity and Gas*
7	Pengadaan Air, Pengelolaan Sampah, Limbah, dan Daur Ulang	1,556	1,752	1,692	1,859	2,013	2,337	2,532	*Water supply, sewerage, waste management and remediation activities*
8	Konstruksi	71,998	72,039	59,164	57,583	52,264	54,476	55,647	*Construction*
9	Perdagangan Besar dan Eceran, Reparasi Mobil dan Motor	518,627	548,285	530,669	601,408	656,431	686,505	692,036	*Wholesale and retail trade; repair of motor vehicles and motorcycles*
10	Transportasi dan Pergudangan	34,756	39,601	36,595	37,424	39,102	46,805	50,126	*Transportation and storage*
11	Penyediaan Akomodasi dan Makan Minum	39,253	45,138	50,623	58,603	61,393	67,097	71,718	*Accommodation and food service activities*
12	Informasi dan Komunikasi	7,651	7,358	7,671	6,314	7,582	7,607	8,582	*Information and communication*
13	Jasa Keuangan dan Komunikasi	22,755	20,288	15,041	12,385	13,257	16,690	14,601	*Other financial and communication*
14	Real Estate	20,452	21,898	20,213	18,312	17,717	18,107	20,001	*Real estate*
15	Jasa Perusahaan	32,787	37,291	31,049	30,451	34,332	36,300	38,258	*Business Services*
16	Administrasi Pemerintahan, Pertahanan, dan Jaminan Sosial Wajib	535	160	100	214	387	238	187	*Public administration and defence; compulsory social security*
17	Jasa Pendidikan	6,285	6,872	7,235	8,294	8,554	9,391	9,553	*Education*
18	Jasa Kesehatan dan Kegiatan Lainnya	10,246	11,718	10,257	11,825	12,537	13,922	14,936	*health and social work activities*
19	Jasa Lainnya	51,106	54,725	56,252	62,620	70,581	82,309	87,360	*Other service activities*
20	Tidak Teridentifikasi	0	264	1	556	0	0	0	*Not Identified*
21	**Jenis Penggunaan**	**1,032,643**	**1,111,340**	**1,091,232**	**1,223,433**	**1,351,249**	**1,460,164**	**1,507,063**	***Type of Credit***
22	Modal Kerja	766,213	800,638	799,226	927,327	1,015,647	1,056,753	1,057,351	*Working Capital*
23	Invetastasi	266,430	310,701	292,007	296,106	335,602	403,411	449,711	*Invetsasi*
24	Tidak Teridentifikasi	0	0	0	0	0	0	0	*Not Identified*
25	**Skala Usaha**	**1,032,643**	**1,111,340**	**1,091,232**	**1,223,433**	**1,351,249**	**1,460,164**	**1,507,063**	***Business Criteria***
26	Mikro	251,336	283,704	247,176	389,895	532,724	662,361	670,275	*Micro*
27	Kecil	312,069	343,792	353,125	459,744	466,706	461,109	498,082	*Small*
28	Menengah	469,237	483,844	490,931	373,794	351,819	336,695	338,706	*Medium*
29	**Kredit dengan Penjaminan Tertentu 2)**	**137,944**	**163,722**	**178,067**	**315,635**	**456,613**	**435,114**	**451,374**	***o/w Credit with Specific Guarantee Scheme 2)***
30	Mikro	74,635	80,689	77,529	197,782	322,007	303,289	310,187	*Micro*
31	Kecil	56,843	75,352	93,996	112,237	133,227	130,679	140,264	*Small*
32	Menengah	6,466	7,681	6,542	5,616	1,378	1,145	923	*Medium*

Catatan:
1) Sejak Juni 2016 termasuk Bank Umum Syariah / Unit Usaha Syariah
2) Pemberian kredit yang dijamin oleh penjamin tertentu yang memenuhi persyaratan.
-Sejak Mei 2014 terdapat perubahan cakupan dan klarifikasi data Dana dan Kredit berkaitan dengan implementasi Laporan Bulanan Bank Umum Syariah (LBUS) berdasarkan Laporan Stabilitas Moneter dan Sistem Keuangan (LSMK). Penjelasan lebih lanjut terdapat di Metadata

Notes:
1) Since June 2016 included Islamic Bank / Shariah Business Unit
2) The extension of credit secured by certain eligible guarantor.
-Since May 2014, data coverage and classification has been enhanced related to the implementation of Islamic Banking Monthly Report (LBUS) based on Monetary and Financial System Stability Report (LSMK). For further explanation please refer to Metadata

Microfinance is defined as financial services in the form of raising funds and providing loans or financing on a small scale with simple procedures designed for the poor or low-income communities (Candra & Zulkarnain, 2024). Internationally, microfinance refers to financial services provided to small businesses or micro-entrepreneurs who generally do not have access to formal banking due to the high transaction fees charged by banking institutions (Hagawe et al., 2023). Microfinance encompasses a wide range of financial services, such as microcredit, microsavings, and microinsurance, which aim to support small businesses and promote financial inclusion (Putra & Asmana, 2023).

Microcredit, as part of microfinance services, provides access to finance to customers with small to medium-sized businesses that tend not to have formal banking relationships. Customers in this category often do not have collateral, steady income, or complete administrative documents, thus requiring simpler requirements (Hansen et al., 2020). Besides microcredit, microfinance services also include micro savings and micro insurance. Unfortunately, in Indonesia, microinsurance is still less well known than microcredit, despite its considerable potential in providing protection for low-income people (Wanambisi & Bwisa, 2013).

Microfinance has proven to be an effective tool in supporting real sector development and improving people's welfare. For example, microfinance programs in several developing countries have shown that access to microfinance services can help small entrepreneurs increase income, create jobs, and support local economic growth (Saputri et al., 2023). In Indonesia, the government through Bank Rakyat Indonesia (BRI) has been a pioneer in the provision of microfinance services since the 19th century, continuing to offer microcredit to the community until today. This program has been instrumental in expanding financial inclusion across Indonesia (Ar et al., 2024).

However, challenges remain in the development of microfinance in Indonesia. Some of these include the high risk of default, lack of financial literacy among clients, and inequitable access to microfinance services in remote areas (Hajar, 2024). Therefore, a more inclusive and sustainable strategy is needed to ensure that microfinance services can reach the poor throughout Indonesia. This includes improving financial literacy, developing financial technology, and collaboration between the government and private sector to expand the reach of microfinance services (Asmana et al., 2024).

Microfinance in Indonesia has a long history that is divided into two main periods, namely the colonial era and the independence era. During the Dutch colonial period, the financial system was dominated by the Dutch East Indies government through the establishment of several large banks. One important milestone was in December 1895, when Raden Bei Wiriaatmadja established the Hulp en Spaarbank der Inlandsche Bestuurs Ambtenaren in Purwokerto, which became the forerunner of the People's Credit Bank. This institution aimed to provide financial assistance to native employees with simple procedures. This initiative was reinforced by De Wolf van Westerrode, who then expanded the People's Credit Bank to various regions in Java (Ferdyan & Hartawan, 2024).

During the same period, villages in Java established Lumbung Desa, a rice-based savings and loan institution as a credit instrument. Lumbung Desa evolved into Badan Kredit Desa (BKD) in 1904, which continues to serve rural communities today. After Indonesia's independence, the Algemene Volkscredietbank (AVB) formed during the colonial period was merged into Bank Rakyat Indonesia (BRI), which became a pioneer microfinance service provider in Indonesia (Hermanto et al., 2020).

During the Soeharto administration, attention to rural development increased. The government established rural banks (BPRs) in all provinces and introduced programs such as Mass Guidance (Bimas) that provided subsidies to farmers through institutions such as KUD and BUUD. Other microcredit programs, such as Kredit Investasi Kecil (KIK) and Kredit Modal Kerja Tetap (KMKP), helped farmers and small businesses to gain access to capital. This strategy shows that microfinance not only serves economic needs, but also becomes an instrument of social policy (Hidayatullah et al., 2024).

The long history of microfinance has resulted in various types of microfinance institutions (MFIs) in Indonesia. These institutions include Lembaga Dana Perkreditan Pedesaan (LDKP), Lembaga Kredit Desa (LPD) in Bali, and Lumbung Pitih Nagari in West Sumatra. However, overlapping policies, regulations, and authorities between institutions are a major challenge in the management and development of MFIs. Competition with modern banking institutions such as BRI and BPR also makes it difficult for many MFIs to survive sustainably (Mushtaq & Bruneau, 2019).

In addition, the lack of accurate data on the number and condition of MFIs makes it difficult to formulate effective policies. Research conducted by foreign institutions is often the basis for predicting the presence of MFIs, although it is seasonal and does not include regular monitoring (Shak et al., 2024). For example, in Bali there are more than five types of MFIs in one village, including KUD, KSP, and BRI micro units. This makes it difficult to map and evaluate the success of microfinance services in Indonesia.

Several previous studies have contributed significantly to understanding the role of microfinance in reducing poverty. (Cull & Hartarska, 2023) examined the relationship between financial inclusion and economic development, showing that microfinance is effective in expanding access to financial services for the poor, especially in developing countries. This research emphasizes the importance of sustainability of microfinance institutions (MFIs) to achieve optimal results. However, this study does not specifically address the regulatory and supervisory challenges faced by MFIs in Indonesia (Saefullah & Hajar, 2022).

(Cull & Morduch, 2018) evaluated microfinance business models in various countries, including Indonesia, and found that subsidy-based models often face difficulties in maintaining sustainable operations. This study highlights the importance of operational efficiency in maintaining MFI sustainability. However, they did not review in depth the socio-cultural factors that affect the success of microfinance programs in Indonesia.

(Omowole et al., 2024) discussed the role of Bank Rakyat Indonesia (BRI) in supporting financial inclusion through microcredit. They show that BRI's success is supported by its extensive network and strong marketing strategy. However, this study did not discuss the effect of microfinance on the real sector at the rural level. A noticeable analytical gap from previous studies is the lack of attention to Indonesia's specific social, cultural, and regulatory aspects, as well as how microfinance can more effectively support real sector development. This research fills the gap by exploring the regulatory, social integration, and implementation challenges of microfinance programs at the local level. It provides a new perspective on developing a more inclusive and sustainable microfinance in Indonesia.

2. METHOD

This research uses a normative juridical approach, which aims to examine the legal aspects related to the activity model of microfinance institutions (MFIs) in Indonesia, especially the legal issues that have been identified. The normative juridical approach involves analysis of positive law, legal principles, legal systematics, legal history, and comparative legal research (Firmanto et al., 2024).

The approach method used is the normative legal approach method, which includes research on the discovery of positive law, legal principles, legal systematics, legal history and comparative legal research. This research was conducted by examining literature or secondary data obtained from libraries and related institutions that are competent with this research. As for normative legal research using secondary data in the form of primary legal materials, secondary legal materials and tertiary legal materials. In this study, the legal aspects of the LKM activity model in Indonesia will be studied, especially regarding the legal problems that have been identified.

This research was conducted over three months, from June to August 2024. During this period, research activities included data collection from the literature, analysis of legal documents, and interviews with relevant resource persons. The research object includes legal aspects related to MFI operations in Indonesia, with a focus on regulation, supervision, and sustainability of the MFI model. This research examines secondary data from various sources, including primary legal documents (laws and regulations), secondary legal documents (related literature and research results), and tertiary legal documents (legal dictionaries and encyclopedias).

The specification of this research is analytical descriptive, namely making a systematic description of the facts including describing the regulations. Thus, this research will describe various legal problems obtained through the discovery of positive law, the discovery of legal principles and the discovery of law in concreto against LKM which aims to obtain a comprehensive and systematic picture through the analysis process using legal principles, legal principles and the understanding of LKM law.

The data analysis method used in this research is the qualitative normative analysis method. Normative analysis because this research is based on applicable laws and regulations as positive legal norms, while qualitative is a research method that focuses on obtaining descriptive data, through what is stated by the resource person both verbally and in writing and the reality that occurs.

Data obtained through: Library Research: Collecting secondary data from books, journals, regulations, and other legal documents relevant to MFIs. Interview: Exploring information from resource persons, such as MFI managers, academics, and legal practitioners, to complement the normative study. And Documentation: Analyzing official documents, including laws and regulations governing MFIs in Indonesia, such as Law No. 1 Year 2013 on Microfinance Institutions.

The collected data were analyzed using qualitative normative methods (Nartin et al., 2024). The normative method is used to review applicable laws and regulations as positive legal norms. The qualitative approach was used to understand and explain descriptive data obtained from sources, documents, and the reality that occurred. The analysis process involved the following steps:

1. Data Classification: Classify data based on main themes, such as legal regulations, operational implementation, and legal barriers of MFIs.
2. Legal Interpretation: Interpret legal rules, legal principles, and legal definitions related to MFIs.
3. Analytical Descriptive Analysis: Make a systematic description of relevant legal regulations, analyze the relationship between positive law and its application in the field, and provide a comprehensive picture of legal issues related to MFIs.

With this approach, the research is expected to comprehensively describe various MFI legal issues and provide relevant recommendations for the development of regulations and MFI operational models in Indonesia.

3. RESULT AND DISCUSSION

This research found several key findings related to the legal and operational aspects of microfinance institutions (MFIs) in Indonesia based on the normative juridical method. Data was analyzed from legal documents, interviews with practitioners, and literature review, providing a comprehensive picture of regulations, implementation, and challenges faced by MFIs. The following are the main findings of this study:

1. MFI Regulations and Implementation

Based on the analysis of legal documents, it is found that Law No. 1 Year 2013 on Microfinance Institutions is the main legal basis in regulating MFI operations. However, its implementation still faces obstacles, such as overlapping authority between local and central government, as well as lack of regulatory harmonization between MFIs and other financial institutions.

Regulatory Aspects	Findings
Main Law	Law No. 1 Year 2013 on MFIs
Overlapping Regulations	The authority between central and local government is not clear.
Harmonization of Regulations	Not yet fully integrating MFIs with local government.

2. Role of MFIs in Supporting the Real Sector

MFIs play a significant role in supporting the real sector, especially for small businesses in rural areas. Of the 20 interviewees, 70% stated that microcredit from MFIs helped them increase their business capacity. However, the main challenge lies in the accessibility of services in remote areas.

Operational Aspects	Findings
Microcredit Benefits	70% of business owners claimed to benefit from microcredit.
Service Accessibility	MFIs in remote areas face service distribution constraints
Financing Focus	Majority of financing is directed to agriculture and trade sectors

Micro Credit helps LKM actors in the New Order era, micro credit is widely applied in the form of Village Unit Cooperatives (KUD), even loans in the form of KCK (Kredit Candak Kulak) and KIK (Small Investment Credit) but over time micro financial institutions are only focused on micro business communities. These micro financial institutions are known as LKM. LKM has a different character from other financial sector businesses. The existence of LKM is not only to seek profit, but also to increase income and welfare of the people and help increase economic empowerment and community productivity by facilitating poor and low-income communities, especially micro businesses. This can be seen through the types of LKM business activities which include providing loans or financing to micro-scale businesses, savings management, and business development consulting services which ultimately lead to community empowerment.

3. Constraints Faced by MFIs

Field findings show that MFIs face three main constraints: lack of operational capital, low financial literacy of clients, and competition with modern financial institutions such as commercial banks and BPRs. As many as 60% of respondents stated that limited capital is the biggest challenge for MFIs to grow.

MFI constraints	Findings
Limited Operating Capital	60%
Low Financial Literacy	25%
Tight Competition	15%

Tight competition and overlapping policies have made many MFIs unable to compete, so they have to stop their business or just remain in name. As an illustration, in a village in Bali Province, there can be more than five to seven types of MFIs or banks targeting the micro segment, including LPD, KUD, Multipurpose Cooperatives (KSU) or Savings and Loan Cooperatives (KSP) established by the community, BPR, Teras BRI (BRI micro unit), and Danamon Simpan Pinjam (DSP).

The difficulty of grouping microfinance institutions and types of microfinance services makes mapping, monitoring and evaluation of these financial services difficult. Overlapping regulations, authorities and broad scope of microfinance institution services also contribute to the difficulty of implementing the right development strategy for MFIs. This situation causes the level of business sustainability or sustainability of MFIs and microfinance programs to be low. Only a few MFIs are able to survive and compete well with other MFIs and more modern types of banking services.

The absence of definite data regarding the number and condition of these institutions makes it difficult for the author to present the accuracy regarding the number of these institutions. Many institutions are under the guidance of the provincial government, but there is no definite data from each regional government regarding the existence of microfinance institutions in their area.

4. MFI Sustainability Strategies

To overcome these challenges, MFIs have adopted several strategies, such as establishing partnerships with local governments and non-governmental organizations and improving training for clients. Of the respondents interviewed, 80% stated that financial literacy training is very helpful for them in managing their business.

Sustainability Strategy	Findings
Partnership	MFIs partner with local government to improve operational capacity
Financial Literacy Training	80% of clients consider the training helpful

The findings suggest that MFIs have great potential in supporting the real sector and financial inclusion in Indonesia. However, challenges such as lack of regulatory harmonization, capital constraints, and financial literacy need to be addressed to ensure the sustainability of MFI operations. With collaboration between the government, MFIs, and the private sector, the microfinance system can be more effective in reducing poverty and supporting sustainable development.

The problem that occurs in Indonesia is the large number and variety of microfinance institutions and types of microfinance services. This makes mapping, monitoring and evaluation of these financial services difficult to do. Overlapping regulations, authorities and broad scope of microfinance institution services also contribute to the difficulty of implementing the right development strategy for MFIs. This situation causes the level of sustainability of MFIs and microfinance programs to be low. Only a few MFIs are able to survive and compete well with other MFIs and more modern types of banking services

The results show that microfinance institutions (MFIs) in Indonesia play an important role in supporting financial inclusion and the real sector, especially in rural areas. However, the implementation of MFI regulations and operations still face significant challenges. This finding is relevant to research (Andriansyah et al., 2024) which emphasizes that the success of microfinance is strongly influenced by an effective regulatory framework and the sustainability of financial institutions. In the Indonesian context, Law No. 1 Year 2013 on MFIs is the main legal basis, but the overlapping authority between central and local governments is still a major obstacle in the management of MFIs (Ubed & Mugiyati, 2024)

This research also reveals that microcredit has a positive impact on small business development, as confirmed by Cull et al. (2019), who found that microfinance helps small entrepreneurs increase income and create jobs. In this study, 70% of respondents stated that microcredit helped them to increase their business capacity, especially in the agriculture and small trade sectors. However, accessibility of MFI services in remote areas remains a challenge, in line with the findings of (Aditya et al., 2025), which stated that the distribution of microfinance services is often uneven.

In addition to the benefits, this study found the main constraints of MFIs, namely limited operational capital, low financial literacy of customers, and fierce competition with modern financial institutions (Prabowo, 2024) also noted that the sustainability of MFI operations requires strong capital support and institutional capacity strengthening. These constraints affect the ability of MFIs to compete with commercial banks and other financial institutions, especially in urban areas. Low financial literacy among clients adds to the complexity of the problem, as mentioned by which highlights the importance of financial education to improve the effectiveness of microfinance programs.

Sustainability strategies implemented by MFIs, such as establishing partnerships with local governments and providing financial literacy training, have shown positive results. As many as 80% of respondents consider the training helps them manage their business better. This finding supports research (G & Gustiana, 2025), which states that financial training and strengthening client capacity are key elements for microfinance success.

Compared to previous studies, this research makes an additional contribution by highlighting specific regulatory challenges in Indonesia and the importance of collaboration between the government, MFIs, and the private sector to improve service accessibility. In addition, this study emphasizes the need for a more integrated strategy to address policy overlaps and utilize the full potential of MFIs. Thus, the findings can serve as a basis for policy improvement and development of more inclusive and sustainable microfinance programs.

Based on Law No. 1 Year 2013 on Microfinance Institutions (MFIs), the financial sector in Indonesia has a strategic role in driving national economic growth, especially among the poor and low-income communities. The development of the financial sector, including non-bank financial institutions such as MFIs, requires strengthening in institutional, regulatory, and human resources aspects (Siregar & Wahyudi, 2022).

MFIs play a significant role in providing access to microfinance, which aims to increase community economic empowerment through loans, savings management, and business advisory services.

The main characteristic of MFIs that distinguishes them from other financial institutions is their focus on empowering the poor and micro enterprises (Hakim et al., 2024). MFIs do not only seek profit, but also aim to improve the welfare of the community. In its operations, MFIs provide services such as microfinance, micro-savings management, and sharia-based activities, such as the management of zakat, infaq, sadaqah, and waqf funds. This supports the role of MFIs as an instrument of inclusive and sustainable economic empowerment (Anita et al., 2024).

However, there are a number of restrictions on MFI operations regulated by law, such as the prohibition of accepting deposits in the form of demand deposits, conducting transactions in foreign currencies, or providing loans to other MFIs outside the district/city area. This regulation aims to ensure the stability and focus of MFI operations in accordance with its mandate (Rahmadewi et al., 2024).

From a regulatory perspective, MFIs are required to have a business license from the Financial Services Authority (OJK) with certain requirements, including organizational structure, capital, and feasibility of work plans. This business license also applies to institutions that have been operating before the MFI Law came into effect, such as Bank Desa, Lumbung Desa, and Baitul Maal wa Tamwil (BMT). However, the implementation of this regulation still faces obstacles, including the lack of harmonization between central and local policies, and the diverse operational capacity of MFIs (Izza et al., 2024).

As of February 2016, 34 MFIs have obtained official licenses, up from 20 in January 2016. However, this number is still relatively small compared to the potential number of MFIs operating in Indonesia. Limited start-up capital, complex administrative requirements, and difficulties in facing competition from modern financial institutions are the main challenges for the sustainability of MFIs (Ridwan et al., 2024). Under certain conditions, MFIs can be dissolved if liquidity and solvency problems cannot be resolved. OJK has the authority to revoke the business license and order the dissolution through the General Meeting of Shareholders or Members Meeting. This step is important to maintain public confidence in the stability and integrity of the microfinance sector. MFIs have great potential in supporting community economic empowerment, but regulatory strengthening, policy harmonization, and operational capacity building are needed to ensure its sustainability in the future.

4. CONCLUSION

This study concludes that Microfinance Institutions (MFIs) have a significant role in supporting financial inclusion and community economic empowerment, especially for the poor and micro-entrepreneurs. MFIs provide various financial services, such as microfinance, micro savings, and business advisory services, which aim to improve community welfare. Regulations under Law No. 1 of 2013 on MFIs provide an important operational foundation, but implementation still faces challenges, including policy harmonization between central and local governments, limited capital, and low financial literacy of clients. The findings suggest that regulatory strengthening, technical support, and operational capacity building are needed to improve MFI sustainability. Under certain conditions, MFIs with solvency and liquidity issues can be dissolved by OJK to maintain the stability of the microfinance sector. As a suggestion, the government needs to encourage harmonization of regulations between central and local governments and provide technical support to MFIs in the form of training and capital incentives. In addition, financial literacy for the community needs to be improved so that they can optimally utilize microfinance services. Collaboration between the government, MFIs, and private sector is expected to create a more inclusive and sustainable microfinance system.

In addition, in an effort to provide financial services, which are intended for low-income communities who do not have access to banking financial institutions. LKM can bridge the problem of micro-enterprise access to capital needed in business development. LKM has a different character from other financial sector businesses, because it is not solely aimed at seeking profit. LKM business activities can be carried out conventionally or based on sharia, including providing loans/financing to a micro-scale business for capital needs in business development, and managing savings as an effort to raise awareness in the community to like saving, while LKM also provides business development consulting services whose goal is community empowerment. To provide legal certainty for the community using LKM services, LKM institutions are regulated in the LKM Law, according to the law LKM must be a legal entity of a Cooperative or Limited Liability Company. Guidance, regulation, and supervision as well as licensing of LKM are carried out by the OJK. If conducting business activities outside the district/city area or have met the requirements as stipulated in the Financial Services Authority Regulation, then the LKM changes into a People's Credit Bank (BPR).

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