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## **Strengthening the Role of BPRS in Supporting MSMEs: Regulatory Perspective and Legal Challenges During and After the Pandemic**

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### **Abstract**

This study examines the strategic role of Sharia People's Financing Banks (BPRS) in supporting micro, small and medium enterprises (MSMEs) as a driver of Indonesia's economic recovery in the aftermath of the Covid-19 pandemic. Despite having a smaller share of total financing than Islamic Commercial Banks, BPRS plays a crucial role in reaching underserved microeconomic segments. Previous studies have shown that MSMEs are the backbone of the Indonesian economy, yet their access to financing remains limited. This research uses a qualitative method with a field approach through observation, in-depth interviews, and document analysis in selected regions. The findings show that BPRS financing has significantly contributed to MSME resilience and job creation, yet the sector still faces regulatory and policy challenges. Therefore, optimizing BPRS' contribution requires legal frameworks that support risk mitigation, sustainability, and inclusive economic growth.

**Keywords:** BPRS, Economic Growth, Covid-19 Pandemic

### ***Abstrak***

*Penelitian ini mengkaji peran strategis Bank Pembiayaan Rakyat Syariah (BPRS) dalam mendukung usaha mikro, kecil, dan menengah (UMKM) sebagai penggerak pemulihan ekonomi Indonesia pasca pandemi Covid-19. Meskipun kontribusi pembiayaan BPRS secara nominal lebih kecil dibandingkan Bank Umum Syariah (BUS), peran BPRS sangat penting dalam menjangkau segmen ekonomi mikro yang belum terlayani. Studi-studi sebelumnya menunjukkan bahwa UMKM merupakan tulang punggung perekonomian nasional, namun masih menghadapi keterbatasan akses terhadap pembiayaan. Penelitian ini menggunakan metode kualitatif dengan pendekatan lapangan melalui observasi, wawancara mendalam, dan analisis dokumen di beberapa wilayah terpilih. Hasil penelitian menunjukkan bahwa pembiayaan oleh BPRS berkontribusi signifikan terhadap ketahanan UMKM dan penciptaan lapangan kerja, namun sektor ini masih menghadapi tantangan regulasi dan kebijakan. Oleh karena itu, optimalisasi kontribusi BPRS memerlukan kerangka hukum yang mendukung mitigasi risiko, keberlanjutan, dan pertumbuhan ekonomi yang inklusif.*

***Katakunci:*** BPRS, Pertumbuhan Ekonomi, Pandemi Covid-19

### **Introduction**

The Covid-19 pandemic is still having a significant impact in various parts of the world, including Indonesia. The impact of this pandemic is felt in various sectors, especially the economic and financial sectors, including Islamic bankin.<sup>1</sup> As a financial institution that facilitates transactions based on sharia principles, Islamic banks play a role in ensuring that every transaction is in accordance with Islamic teachings. Islamic banks are expected to maintain a balance between financial and social performance and contribute positively to reducing poverty, preserving the environment, supporting social justice, improving health, education and spiritual values.<sup>2</sup>

As intermediary institutions, banks must operate optimally to support the smooth running of the economy. When the banking industry is in a healthy condition, the allocation of economic resources can be done more efficiently<sup>3</sup>. Public trust in Islamic banks as an alternative solution to the financial crisis continues to increase. Considering that Indonesia is the country with the largest Muslim population in the

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<sup>1</sup> Mohammad Sofyan, "Kinerja BPR Dan BPRS Pada Masa Pandemi COVID-19," *The 2nd Seminar Nasional ADPI Mengabdikan Untuk Negeri Pengabdian Masyarakat Di Era New Normal* 2, no. 2 (2021), p. 6–12.

<sup>2</sup> Lucky Nugroho et al., "The Urgency of Allignment Islamic Bank to Increasing the Outreach (Indonesia Evidence)," *International Journal of Economics and Financial Issues* 7, no. 4 (2017), p. 283–291.

<sup>3</sup> Sugeng Haryanto, "Profitability Identification of National Banking Through Credit , Capital , Capital Structure , Efficiency , and Risk Kredit , Permodalan , Struktur Modal , Efisiensi Dan Tingkat," *Jurnal Dinamika Manajemen* 7, no. 1 (2016), p. 11–21.

world, where 87 per cent of the population is Muslim,<sup>4</sup> Islamic banking is expected to contribute significantly to national economic growth. Until 2020, Islamic banking in Indonesia has developed with the existence of 14 Islamic Commercial Banks (BUS), 20 Islamic Business Units (UUS), and 163 Islamic People's Financing Banks (BPRS)<sup>5</sup>. There are 627 BPRS branches spread throughout Indonesia, with 89 BPRS or around 55 per cent of the total number of BPRS located in Java.

BPRS is part of the Islamic banking system with a different market segmentation from BUS and UUS. Based on regulations, BPRS is encouraged to allocate more resources to the Micro, Small and Medium Enterprises (MSMEs) sector, which is often unreachable by large banks<sup>6</sup>. MSMEs dominate the business sector in Indonesia and play an important role in driving regional economic growth. MSMEs also absorb 99.9 per cent of the workforce in Indonesia, so the increase in the production of goods and services in a region is highly dependent on the financing provided by the banking sector. The greater the funds channeled, the greater the production generated, which in turn will increase regional income and contribute to national economic growth. MSMEs contribute up to 60.3 per cent to economic growth and in recent years have been the focus of the government's capital strengthening programme<sup>7</sup>.

As a country with a large population and a Muslim majority, it should be noted that until now there is no Islamic bank in Indonesia that is able to cover all islands and serve the financial needs of people in all regions<sup>8</sup>. Islamic financial institutions, including BPRS, are expected to play a role in supporting the economic independence of the community through financing MSMEs. The MSME sector has strong resilience to economic crises and plays a significant role in employment and increasing Gross Domestic Product (GDP). In addition, MSMEs are one of the government's efforts in poverty alleviation, as stipulated in Law No. 20/2008 on Micro, Small and Medium Enterprises<sup>9</sup>.

Increased investment and additional business capital from Islamic banking will encourage increased production, which in turn will increase the income of MSMEs. This increase in production also has the potential to expand businesses, create new jobs, reduce unemployment, and increase per capita income. With more

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<sup>4</sup> Mahbub Setiawan, *Islamisasi Nusantara: Dari Episteme Ke Rezim Kebenaran* (Jawa Timur: Academia Publication, 2023).

<sup>5</sup> Haryanto, "Profitability Identification of National Banking Through Credit , Capital , Capital Structure , Efficiency , and Risk Kredit , Permodalan , Struktur Modal , Efisiensi Dan Tingkat."

<sup>6</sup> Mauizhotul Hasanah, Faris Kurnia Hakim, Siti Zulaikha, "The Effect of Islamic Rural Banks (BPRS) on Regional Economies in Java," *Jurnal Ekonomi* 24, no. 2 (2019), p. 256.

<sup>7</sup> Mardhiyaturrositaningsih, "Kinerja Perbankan Syariah Di Masa Pandemi Covid-19 : Studi Kasus Pada BPRS Di Jawa Barat," no. June (2021), p. 92–112.

<sup>8</sup> Nugroho et al., "The Urgency of Allignment Islamic Bank to Increasing the Outreach (Indonesia Evidence)."

<sup>9</sup> A. Tanjung, H., Perwaatmadja, dan Karnaen, *Bank Syariah: Teori, Praktik, Dan Peranannya* (Jakarta: Celestial Publishing, 2007).

labour absorbed, people's purchasing power will increase, which in turn supports national income growth<sup>10</sup>. As part of Islamic financial institutions, BPRS has a primary focus on funding and financing the real sector, with the aim of uplifting the community's economy and driving Indonesia's economic growth<sup>11</sup>.

Referring to the various facts above, this study is important in an effort to understand and optimise the transformation of the strategic role of BPRS in supporting the improvement of the national economy, especially in facing the challenges arising from the Covid-19 pandemic and the dynamics of economic change in the future. As an Islamic financial institution with a different market segmentation from commercial banks, BPRS has great potential to support the growth of MSMEs, which are the backbone of the Indonesian economy. In the midst of the pandemic, MSMEs have shown relatively strong resilience and serve as an important component in national economic recovery. With a deeper understanding of the role of BPRS, this study is expected to provide relevant strategic recommendations to face future economic challenges, such as digitalisation of services, increased competitiveness, and crisis resilience. The results of this study are expected to contribute significantly to the development of Islamic banking policies and practices in Indonesia, while strengthening the role of BPRS in supporting sustainable national economic growth.

Although the role of BPRS in supporting MSME financing has been regulated such as through Law No. 21 of 2008 on Islamic Banking and OJK Regulation No. 35/POJK.03/2018 on Sharia Rural Banks optimizing its contribution still faces various challenges. One of the main obstacles is the limited adaptability of existing regulations to meet the needs of MSMEs during times of crisis, as well as the lack of policy integration across sectors. This is consistent with the findings of Trimulato who noted that the success of BPRS in channeling sharia-compliant financing is highly influenced by the accuracy of regulatory frameworks and the legal protection afforded to micro-entrepreneurs<sup>12</sup>. On the other hand, the study by Hassan dan Aliyu, highlights that Islamic banking needs to more actively develop its social function through regulatory designs that strengthen the real sector, especially MSMEs, so that it can contribute directly to sustainable economic growth<sup>13</sup>.

Therefore, examining the strategic role of BPRS is essential to understand how current policies and regulations can effectively respond to the real financing needs of MSMEs during times of crisis and recovery. This study is relevant as it

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<sup>10</sup> Tanjung, H., Perwaatmadja, dan Karnaen.

<sup>11</sup> Rifa'i and Achmad, "Peran Bank Pembiayaan Rakyat Syariah Dalam Mengimplementasikan Keuangan Inklusif Melalui Pembiayaan UMKM Achmad Rifa' i Latar Belakang Indonesia Merupakan Salah Satu Negara Yang Diprediksi Beberapa Tahun Mendatang Akan Menjadi Bagian Dari 5 Besar Negara," *Journal of Islamic Economics and Business* 2, no. 2 (2017), p. 177–200.

<sup>12</sup> Trimulato Trimulato, "The Role Of Sharia Banking To Recover SMEs During Covid-19 Pandemic," *Al-Masharif: Jurnal Ilmu Ekonomi Dan Keislaman* 9, no. 1 (2021), p. 58–75.

<sup>13</sup> M. Kabir Hassan and Sirajo Aliyu, "A Contemporary Survey of Islamic Banking Literature," *Journal of Financial Stability* 34 (2018), p. 12–43.

focuses on the legal and institutional aspects of the Islamic banking system, particularly in the context of empowering the lower-income segments of society in the post-pandemic era.

This research was conducted in Lampung Province as well as several provinces with the largest number of BPRS, such as Banten, Central Java, and East Java, with a focus on BPRS that implement business strategies in the MSME sector, which is the backbone of Indonesia's economic growth. Through a field study approach, this research makes an important contribution to the development of Islamic banking policies in encouraging national economic growth through MSME empowerment.

This research uses a qualitative research method with a descriptive-exploratory nature that aims to identify and understand the transformation of the strategic role of BPRS in supporting the improvement of the national economy amid the pandemic and in facing future challenges. The approach used is a case study of several BPRS in areas with a significant number of BPRS, such as Lampung, Banten, Central Java and East Java Provinces. Data were collected through in-depth interview techniques with BPRS managers, observation, and document analysis related to business strategies and Islamic banking policies. Data analysis was carried out using thematic analysis<sup>14</sup>, which identifies the main themes related to the strategic role of BPRS in empowering MSMEs and adapting to economic dynamics in the pandemic era and the future, so that relevant recommendations can be formulated for the development of Islamic banking policies.

### **Economic Growth Theory**

Economic growth is an important indicator in assessing the success of a country's development, which is shown through changes in national output<sup>15</sup>. Adam Smith defined economic growth as the process of increasing the production and distribution of economic goods in society, driven by the division of labour and increased efficiency<sup>16</sup>. Meanwhile, Todaro and Smith see economic growth as an increase in a country's per capita income over a period of time, reflecting increased productivity and living standards. According to them, economic growth is influenced by capital accumulation, population growth, and technological progress<sup>17</sup>. Simon Kuznets adds that long-term economic growth depends on increasing economic capacity through technological innovation and institutional change<sup>18</sup>.

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<sup>14</sup> Sharan B. Merriam and Elizabeth J. Tisdell, *Qualitative Research: A Guide to Design and Implementation* (San Francisco: John Wiley & Sons, 2015).

<sup>15</sup> Laksmi Yustika Devi et al., "Model Sosial-Ekonomi Dan Ketahanan Pangan Rumah Tangga Di Indonesia," *Jurnal Ekonomi Dan Pembangunan* 28, no. 2 (2020), p. 103–15.

<sup>16</sup> Adam Smith, *An Inquiry Into the Nature and Causes of the Wealth of Nations* (London: W. Strahan and T. Cadell, 1809, n.d.).

<sup>17</sup> Stephen C Todaro, Michael P. and Smith, *Economic Development* (UK: Pearson Education Limited, 2003).

<sup>18</sup> Simon Kuznets, *Modern Economic Growth: Rate, Structure and Spread* (New Haven: Yale University Press, 1966, n.d.).

Referring to the above opinions, it can be concluded that economic growth reflects the ability of a country to improve the welfare of its people. Various views from experts show that factors such as efficiency, capital accumulation, population growth, technological progress, as well as innovation and institutional change play an important role in promoting sustainable economic growth. By considering these factors, a country can optimise its potential to achieve inclusive and sustainable development.

Theories of economic growth are divided into classical and modern<sup>19</sup>. The classical theory, supported by economists such as Adam Smith and David Ricardo, relies on the free market mechanism as the main driver of economic growth<sup>20</sup>. In contrast, modern theories recognise the importance of government intervention to address market failures. The Harrod-Domar theory, as part of the modern theory, highlights the importance of investment in increasing production capacity<sup>21</sup>. Any increase in capital stock can increase potential output, but actual output depends on aggregate demand<sup>22</sup>.

In Islam, economic growth is defined as the continuous increase of the right factors of production and contributes to human welfare. According to Al-Ghazali, human welfare includes fulfilment of physical needs, mental development and spiritual purification<sup>23</sup>. Although Al-Ghazali did not directly mention the concept of economic growth, Islamic economists support the concept of comprehensive growth, which includes the economic dimension. Heidar Naqvi adds that growth in Islam involves both moral-spiritual and material aspects, with an emphasis on equitable distribution of wealth and balance between generations<sup>24</sup>.

Economic growth in the Islamic perspective is different from the conventional approach, as it is based on sharia principles that emphasise social welfare, justice and the avoidance of exploitation. In Islamic economics, economic growth is defined as an increase in welfare that includes material and spiritual aspects, with the aim of achieving the common good.<sup>25</sup>

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<sup>19</sup> M. L. Jhingan, *The Economics of Development and Planning* (Delhi: Vrinda Publications, 2006).

<sup>20</sup> Boediono, *Ekonomi Indonesia* (Bandung: Mizan, 2017).

<sup>21</sup> Zainul Bahri and Vinni Aprilianti, "Menuju Kesejahteraan Berkelanjutan Pemahaman Terhadap Pertumbuhan Ekonomi Klasik, Neoklasik, Islam, Green Economy, Dan Blue Economy, p. 9; See Also Allya Salsa Bilatul Kh, Diajeng Anugrah Cantika Sari, and Fatkurohman Nur Rangga, "Modernisasi Melalui Pemb," *Makassar: Nas Media Pustaka*, 2023.

<sup>22</sup> Mudrajad Kuncoro, *Ekonomi Pemba- Ngunan: Teori, Masalah Dan Kebijakan* (Yogyakarta: UPP AMP YKPN, 2003).

<sup>23</sup> Ihya' Ulumuddin Abu Hamid al-Ghazali, *Jilid III (Beirut: Dar Al-Fikr, 1989), Lihat Pada Bab Kebahagiaan Dan Kehidupan Baik.*, 1989.

<sup>24</sup> Zaenu Zuhdi, "Pertumbuhan Ekonomi Dalam Perspektif Ekonomi Islam," *Iqtishoduna* 3, no. 2 (2011).

<sup>25</sup> M. Umer Chapra, *Islam and the Economic Challenge* (United Kingdom: The Islamic Foundation, 1992), p. 214–215.

According to Muhammad Umer Chapra, Islamic economics emphasises that growth is not only measured through increased output or income, but also through equitable distribution and fulfilment of people's basic needs. Chapra argues that growth in Islam should create a balance between individual rights and social responsibilities, by minimising inequality and avoiding the accumulation of wealth in certain groups.<sup>26</sup> Abul Hassan adds that economic growth in Islam is closely related to the principles of *tawhīd* (unity), *adl* (justice), and *ihsan* (goodness), which encourage the efficient use of resources to improve community welfare without causing environmental or social damage.<sup>27</sup> Based on these opinions, economic growth in Islam focuses on inclusive and sustainable development, which is not only orientated towards achieving profits, but also on equitable distribution of benefits, improving the quality of life, and preserving the environment. This approach differs from the conventional approach, which often emphasises wealth accumulation without considering social and moral aspects.

### Syariah People's Financing Bank (BPRS)

BPRS is an Islamic bank that does not provide services in payment traffic and cannot be converted into a Rural Bank (BPR). BPRS is prohibited from opening branches or representatives abroad and can only be established by: Indonesian citizens or legal entities whose owners are all Indonesian citizens; local governments; or a combination of both.<sup>28</sup>

BPRS business activities cover several important aspects. BPRS collects funds from the public in the form of deposits, such as savings based on *wadi'ah* contracts or other contracts in accordance with sharia, as well as investments such as deposits based on *mudharabah*.<sup>29</sup> Furthermore, BPRS distributes funds to the community through various forms of financing, including profit-sharing financing based on *mudharabah* or *musyarakah* contracts, financing based on *murabahah*, *salam*, or *istishna'* contracts, *qardh* financing, leasing of goods through *ijarah* or lease purchase contracts, and taking over debt through *hawalah* contracts<sup>30</sup>.

In addition, BPRS can place funds with other Islamic banks under a *wadi'ah* or *mudharabah* contract, transfer funds for the benefit of customers through accounts at Islamic or conventional banks, and provide other Islamic banking products after obtaining approval from Bank Indonesia. However, BPRS is prohibited from conducting activities that are contrary to sharia principles, accepting current account

<sup>26</sup> M. Umer Chapra, *Islam and the Economic Challenge*, p. 215–217.

<sup>27</sup> Abul Hassan, *Principles of Islamic Economics* (New Delhi: New Age International, 1996), p. 132.

<sup>28</sup> Darmawan dan Muhammad Iqbal Fasa, *Manajemen Lembaga Keuangan Syariah* (Yogyakarta: UNY Press, 2020), p. 128; Nurul Ikhsanti et al., *Bank dan Lembaga Keuangan Syariah* (Serang, Banten: Sada Kurnia Pustaka, 2023), p. 66.

<sup>29</sup> Joni Hendra K. et al., *Produk-Produk Lembaga Keuangan Bukan Bank (Perspektif Ekonomi Syariah)* (Riau: CV. Dotplus Publisher, 2024), p. 144.

<sup>30</sup> B A B Ii, "Mardani, Aspek Hukum Lembaga Keuangan Syariah Di Indonesia", (Jakarta: Kencana, 2017), Hlm 1. 1 13," n.d., p. 13–22.

deposits, participating in payment traffic, and conducting foreign exchange transactions without the permission of Bank Indonesia.<sup>31</sup>

BPRS is also not allowed to carry out insurance activities, except as a marketing agent for sharia insurance products, make capital investments outside the institution that manages the liquidity of BPRS, or carry out activities outside those that have been determined. However, BPRS can market insurance products through cooperation with sharia insurance companies, where all related transactions are the responsibility of the insurance company.<sup>32</sup>

As a financial institution for the people, BPRS has a strategic role in supporting the improvement of the national economy, especially through financing the MSME sector which is the backbone of the Indonesian economy. Operating under sharia principles, BPRS provides access to affordable and ethical financing for small businesses that are often underserved by conventional banks. Through various sharia contracts such as *murabahah*, *mudharabah*, and *musyarakah*, BPRS enables MSMEs to grow their businesses without the concern of usury, which is against Islamic principles. In doing so, BPRS contributes to expanding financial inclusion and empowering the local economy.

### Banking Financial Performance

In the context of financial performance, performance reflects the overall picture of the company's condition in a certain period and the results of operational activities and management decisions.<sup>33</sup> Performance assessment involves analysing the financial and economic impact of decisions, comparing those results against other measures as benchmarks.<sup>34</sup> Performance can be measured in two categories: non-financial, which focuses on the quality of service to customers, and financial, which uses financial information such as income statements and balance sheets.<sup>35</sup>

In Islamic banking, the purpose of performance measurement is in line with companies in general, namely to improve and control operations to remain competitive. Performance assessment is important for all stakeholders, including management, customers, business partners and the government. Banks that are able to maintain good performance, especially in terms of profitability and dividend distribution, and comply with prudential banking regulations, have the opportunity

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<sup>31</sup> Lucky Nugroho et al., *Lembaga Keuangan Syariah dari Konsep ke Praktik* (Jawa Barat: Penerbit Widina, 2022), p. 47–48.

<sup>32</sup> Duwi Handoko, *Hukum Perbankan Kontemporer* (Pekan Baru: Hawa dan Ahwa, 2024), 83.

<sup>33</sup> Agung Listiadi, “Pengaruh Kinerja Keuangan Terhadap Nilai Perusahaan Sebagai Manifestasi Pembelajaran Investasi,” *Jurnal Ekonomi Pendidikan Dan Kewirausahaan* 3, no. 2 (2017), p. 197.

<sup>34</sup> Beby Oktania, Putri Kusnadi, and Yuliasuti Rahayu, “Perspektif Balanced Scorecard Sebagai Pengukuran Kinerja Organisasi,” *Jurnal Ilmu Dan Riset Akuntansi* 10, no. 1 (2021), p. 1–15.

<sup>35</sup> Joko Wibowo, “Pengaruh Insentif Finansial Dan Non Finansial Terhadap Kepuasan Kerja Dan Kinerja Karyawan (Riset Empiris Pada Karyawan BRI Wilayah Kantor Cabang Sleman Yogyakarta),” *Jurnal Bisnis Teori Dan Implementasi (JBTI)* 6, no. 2 (2015), p. 159–83.

to increase the value of their shares and third party funds. This reflects the public's trust in the bank.

Samad and Hassan highlighted that the financial performance of Islamic banks is not only assessed in terms of profitability, but also from compliance with sharia principles. They point out that Islamic banks use additional ratios, such as Profit Sharing Ratio and Financing Ratio based on Profit Sharing Principles, as indicators of compliance and contribution to sharia-based economic development.<sup>36</sup>

Based on Financial Services Authority Regulation Number 10/POJK.03/2014, banks are required to conduct an independent health assessment using the Risk-based Bank Rating (RBBR) approach. The assessment is conducted individually or consolidated for Sharia Commercial Banks, while for Sharia Business Units it is conducted individually. The focus of the assessment includes risk profile, good corporate governance, profitability, and capital factors.<sup>37</sup>

### A Review of Previous Studies

The role of Sharia People's Financing Banks (BPRS) in empowering micro, small and medium enterprises (MSMEs) has been widely discussed in the context of Islamic finance development. As part of the Islamic banking ecosystem in Indonesia, BPRS operates under specific regulations, namely Law No. 21/2008 on Sharia Banking and POJK No. 35/POJK.03/2018 concerning Sharia Rural Banks. However, their implementation in supporting MSMEs still faces significant challenges, particularly in times of crisis such as the COVID-19 pandemic.

Beck, Demirgüç-Kunt, and Merrouche<sup>38</sup>, in their comparative study of Islamic and conventional banks, argue that Islamic banks demonstrate greater financial resilience and customer loyalty during periods of economic distress. However, they often lack the regulatory agility needed to respond quickly to the evolving needs of MSME financing. This aligns with the perspective of Abdullah and Dusuki<sup>39</sup> who emphasize that Islamic financial institutions must fulfill the broader objectives of *maqasid al-shariah*—not merely maximizing profit but actively supporting inclusive economic growth and financing the real sector.

From a policy perspective, Kammer et al.<sup>40</sup> suggest that Islamic financial systems must adopt a dual-track approach: ensuring strict adherence to sharia

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<sup>36</sup> Abdus Samad and M Kabir Hassan, "The Performance of Malaysian," *International Journal of Islamic Financial Services* 1, no. 3 (2006).

<sup>37</sup> Otoritas Jasa Keuangan, "POJK No. 10/SEOJK.03/2014 Tentang Penilaian Tingkat Kesehatan Bank Umum Syariah Dan Unit Usaha Syariah," *Otoritas Jasa Keuangan*, 2014, p. 1–14.

<sup>38</sup> Thorsten Beck, Asli Demirgüç-Kunt, and Ouarda Merrouche, "Islamic vs. Conventional Banking: Business Model, Efficiency and Stability," *Journal of Banking and Finance* 37, no. 2 (2013), p. 433–47.

<sup>39</sup> Asyraf Wajdi Dusuki and Abdulazeem Abozaid, "A Critical Appraisal On The Challenges Of Realizing Maqasid Al-Shariaah In Islamic Banking And Finance," *IJUM Journal of Economics and Management* 15, no. 2 (2007), p. 999–1000.

<sup>40</sup> Alfred Kammer et al., "Islamic Finance : Opportunities , Challenges , and Policy Options," n.d.

principles while simultaneously enhancing the regulatory infrastructure to promote innovation, inclusion, and crisis resilience. This is especially relevant for BPRS, which typically serves marginalized and remote communities that conventional banks often overlook.

Therefore, the strategic role of BPRS cannot be separated from the legal and institutional frameworks within which they operate. A responsive and robust regulatory structure is essential to accommodate the specific characteristics and risks of MSME financing. Bridging the gap between legal design and implementation is key to enabling BPRS to function effectively as a financial intermediary, while remaining consistent with both Islamic principles and national economic objectives.

### **Macro and Micro Economic Conditions Before and During Covid-19**

Indonesia's economy is measured by economic growth, which in 2019 reached 5.02% (c-to-c), slightly lower than the government's target due to the global economic slowdown of 2.9%. Factors such as the trade war between the United States and China and Brexit caused global economic instability. The Other Services sector recorded the highest growth of 10.55%. The structure of Gross Domestic Product (GDP) remained almost the same, with the largest contribution coming from the Household Consumption Expenditure Component (PK-RT) at 56.62%, followed by Gross Fixed Capital Formation (PMTB) at 32.33%, and Exports of Goods and Services at 18.41%.<sup>41</sup>

The Covid-19 pandemic has had a significant impact on the Indonesian economy. In April 2020, as many as 1.5 million workers were laid off, mainly in the formal sector, and aviation service sector revenue decreased by IDR 207 billion. The inflation rate was recorded at 2.96% in March 2020, although some commodities experienced deflation. Tax revenue and trade volume also declined, causing investors to delay investment. The International Monetary Fund (IMF) projected global economic growth of -3.0%, while Indonesia's economic growth was recorded at only 2.97% in the first quarter of 2020, far below Bank Indonesia's projection of 4.4%.<sup>42</sup>

With the emergence of Covid-19, Indonesia's economic growth in the first quarter of 2020 only reached 2.1%, down from 5.07% in the same period the previous year. In the first semester of 2020, the economy recorded a contraction of -1.26% with a sharper decline in the second quarter, reaching -5.32%. If the economic recovery does not run optimally, this period is projected to be the worst since 1999.

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<sup>41</sup> BRS, "Berita Resmi Statistik," *Bps.Go.Id* 19, no. 27 (2020), p. 1–8, <https://jakarta.bps.go.id/pressrelease/2019/11/01/375/tingkat-penghunian-kamar--tpk--hotel--berbintang-dki-jakarta-pada-bulan-september-2019-mencapai-58-97-persen.html>.

<sup>42</sup> a Ika Fahrika and Juliansyah Roy, "Dampak Pandemi Covid 19 Terhadap Perkembangan Makro Ekonomi Di Indonesia Dan Respon Kebijakan Yang Ditempuh," *Inovasi* 16, no. 2 (2020), p. 206–13.

The Covid-19 pandemic disrupted global supply chains and various sectors, especially MSMEs.<sup>43</sup> The government took budgetary measures for the health sector and economic recovery, but in the second quarter of 2020, the decline deepened, with the transport sector experiencing the largest contraction of -30.84%. Household consumption, as the main source of growth, contracted by -5.51% in 2020 due to social restrictions and declining purchasing power. The Ministry of Labour reported that 1.4 million workers were affected, mainly in the tourism and textile sectors. To achieve recovery and positive growth in 2021, the government is focusing on increasing spending and consumption while adhering to health protocols.

Indonesia's banking sector is a key pillar of the national economy. During the pandemic, banks are faced with the demand to improve financial performance despite the decline in mobility and economic activity. The government and OJK responded to this challenge by implementing stimulus policies, such as credit relaxation, to maintain financial system stability. State-owned banks supported MSMEs through restructuring programmes for affected debtors. Despite the pressures, Bank Indonesia continues to maintain economic stability by implementing accommodative monetary policies. The Islamic banking sector also needs to adapt to these changes, including digitalising services.<sup>44</sup>

### **BPRS Management of MSMEs**

BPRS has unique characteristics that are influenced by the location of its operations. These geographical differences are reflected in the data published by BPRS across Indonesia, which shows the distinctive characteristics of each region. This uniqueness creates a mutually beneficial banking system between banks and customers, with an emphasis on the fairness of transactions, shared value, and ethical investment. The profit-sharing system applied by BPRS provides fairness and transparency, so that customers avoid the risk of interest which is considered as usury.

BPRS only exists in Indonesia and is established by Indonesian citizens, local governments, or through inter-institutional cooperation. As a financial institution, BPRS aims to provide banking products and services to small and medium-sized enterprises (MSMEs), both in urban and rural areas. In raising funds, BPRS relies on savings and deposits, and is under the supervision of Bank Indonesia as an external supervisory authority tasked with maintaining the integrity of Islamic banking institutions.

BPRS management in Indonesia towards MSMEs has a main focus on increasing access to capital for micro, small and medium enterprises that are often underserved by conventional banks. Based on data from OJK in 2020, around 80%

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<sup>43</sup> Abdurrahman Firdaus Thaha, "Dampak Covid-19 Terhadap UMKM Di Indonesia [The Impact of Covid-19 on MSMEs in Indonesia]," *Jurnal Brand* 2, no. 1 (2020), p. 148–53.

<sup>44</sup> Taufik Akhmad, "Dampak Pandemi Covid-19 Terhadap Pertumbuhan Ekonomi Indonesia Dan Solusi Mengatasinya," *Muttaqien; Indonesian Journal of Multidisciplinary Islamic Studies* 3, no. 1 (2022), p. 67–77.

of the BPRS financing portfolio was channelled to MSMEs, with priorities in the trade, agriculture and home industry sectors. This financing demonstrates the role of BPRS as an Islamic financial institution oriented towards the economic empowerment of small communities, which play a key role in the local and national economy.<sup>45</sup>

BPRS in Indonesia adopts several Islamic financing schemes such as murabahah (sale and purchase), mudharabah (profit-sharing), and musyarakah (co-operation) contracts, which enable MSME players to obtain capital while adhering to sharia principles. The profit-sharing system in mudharabah and musyarakah contracts, for example, is considered fairer because it divides profits according to mutual agreement, and avoids burdensome interest charges. This makes BPRS financing more inclusive and sustainable for MSMEs, many of which operate in rural areas and small towns.

In carrying out its operations, BPRS is not only free from usury practices but also orientated towards customer welfare. There are several fundamental characteristics of BPRS, namely: Elimination of the interest (usury) system; services that focus on the public interest and the achievement of Islamic socio-economic goals; more careful evaluation of financing applications with an equity participation orientation, through the application of the profit-sharing principle; enhancement of the relationship between BPRS and customers through the profit-sharing system; accelerating economic activity in the real sector; and helping customers escape the bondage of usury-based moneylenders. These characteristics emphasise the commitment of BPRS to provide banking services in accordance with sharia principles and contribute to the welfare of the community.

## **BPRS Policies, Roles, and Challenges in Indonesia**

### **1. BPRS Mu'amalah Cilegon**

PT BPRS Baitul Muawanah began operations on 1 September 1994 based on Banking Law No. 7 of 1992 and Government Regulation No. 72 of 1992 on profit sharing banks, under the guidance and supervision of Bank Indonesia. On 14 February 2013, through a notarial deed and approval from the Minister of Law and Human Rights, the bank changed its name to PT BPRS Muamalah Cilegon (Bank Syariah Muamalah).<sup>46</sup> In recent years, the bank has established syndicated financing with BPRS in the Greater Jakarta area, including property financing of up to Rp25 billion, a boarding apartment project near the ITB campus, as well as Umrah and Hajj financing through salary deductions in cooperation with cooperatives and payroll departments. In addition, BPRS Muamalah also offers other products such as

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<sup>45</sup> Otoritas Jasa Keuangan, "Laporan Profil Industri Perbankan Syariah Indonesia," 2020, p. 12–15.

<sup>46</sup> "Profil Perusahaan," Bank Syariah Muamalah, accessed October 30, 2023, <https://banksyariahmuamalah.co.id/profil-perusahaan/>.

mortgage financing, land plots, and teacher certification (Sergu), with a primary focus on MSME financing.<sup>47</sup>

In terms of portfolio, 70% of BPRS Muamalah's *financing* is focused on the MSME sector, including *project financing* for contractors. Cilegon City, known for its many large factories, offers great market potential for BPRS Muamalah. Seeing this opportunity, BPRS Muamalah provides financing to individuals or business entities handling civil projects or contractors. One of the latest projects funded is the Korean chemical company PT Lotte Gentle, which is also evaluated for its project omzer. Although it involves large entrepreneurs, the work on this project is still handled on an MSME scale.

BPRS Muamalah applies two financing patterns, namely *Tijarah* and *Tabarru*. In the *Tijarah* financing pattern, for example in BPRS Lampung region, the portfolio with a 50% ratio is focused on the consumptive sector, while in BPRS Muamalah the portfolio is prioritised for the MSME sector. BPRS Muamalah is ready to take greater risks in financing because it has the potential to generate higher income according to the principle of "*High Risk, High Return*". In the *Tabarru* financing pattern, BPRS Muamalah cooperates with the Community Empowerment House and LAZ Harfa in Banten Province on a national scale, with the support of international funds, such as from Australia, to reduce the impact of usury and create a "moneylender-free village". In this scheme, BPRS Muamalah takes no profit; funds are channelled on a revolving basis and do not need to be returned. The programme, called *Qobul Hasan*, uses strict selection to determine coaching points in a village according to BPRS Muamalah's methods.

The challenges faced by BPRS Muamalah include competition with moneylenders, conventional cooperatives, and mobile banks. *The Qobul Hasan* programme, which has been explained previously, is a solution because it does not apply interest at all and is supported by several companies. However, another challenge arises when the funds provided to community MSMEs are used for consumption purposes. Therefore, education is important so that the funds received can be utilised productively. This programme is supervised and accompanied by BPRS Muamalah, both in terms of operations and production processes. Through this approach, BPRS Muamalah plays a role in advancing customer businesses and encouraging the success of MSMEs.

During the Covid-19 pandemic, BPRS Mu'amalah consistently provided financing for MSMEs even though several other banks experienced difficulties in providing financing due to business closures which caused funds to be allocated only for consumption. BPRS Mu'amalah focuses on supporting MSMEs as partners who play a role in the progress of customer businesses. With the relaxation from the government, BPRS Mu'amalah continues to channel financing funds, making this bank the frontline in supporting MSMEs during the pandemic. Wholesale vegetable

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<sup>47</sup> Interview with Dedi Murdikari, Remedial and AM employee of PT BPRS Baitul Muawanah Cirebon, Cirebon Regency, October 2023.

financing is the main choice in this bank, and despite the pandemic, BPRS Muamalah's financial stability is maintained at a safe level.

Cilegon City, as the fourth richest city in Indonesia with a strong industrial sector, has a large turnover of money. Migrants peddling various products in the city can easily find a market, while locals tend to move elsewhere if there are job opportunities with better prospects, indicating an orientation towards increasing income. BPRS Muamalah is optimistic about the size of the market, despite competition from conventional banks that receive assistance from the government. Unlike other banks, BPRS Muamalah is purely funded by public funds which are then channelled back to the community. A popular trend among customers today is *mosque savings*, which is not for physical development, but for infaq and sadaqah. This trend is growing because the DKM has appointed the community to save in Islamic banks, so that Islamic values are more radiated compared to conventional banks. In addition, the benefits of saving are increasing, and BPRS Muamalah Cilegon provides onsite fund pick-up services.

The role of BPRS is very well received by the community, because the vision of BPRS focuses on the benefit of the people and the principle of the hereafter, not merely worldly profit. BPRS Muamalah Cilegon recorded assets of Rp 60 billion with a target of expanding new branch offices to reach more people. The focus on financing is enlarged due to the high queue of funding from stakeholders, with the priority of financing at 70%. One of BPRS Muamalah Cilegon's programmes is through Rabbani Syariah Cooperative, which channels funds to MSMEs with capital from BPRS Muamalah. In this cooperation, the cooperative receives *ujroh* (fee) while BPRS Muamalah Cilegon acts as supervisor and director.

Data as of 26 June 2022 shows that the number of BPRS Muamalah customers reached 1,636 people, with an allocation of working capital and MSME investment and consumptive financing of 50% each. Working capital was recorded at Rp 16,188,746,666, investment at Rp 1,841,000,000, and consumption financing reached Rp 17,653,567,811.

## **2. BPRS Dana Amanah Surakarta**

BPRS Dana Amanah was inaugurated by Bank Indonesia (BI) on 23 May 2008 AD, coinciding with 17 Jumadil Ula 1429 H, and began operations on 2 June 2008 AD or 27 Jumadil Ula 1429 H. BPRS Dana Amanah went through a licensing process for approximately two years at Bank Indonesia with the main objective of increasing shared prosperity through Islamic banking practices. BPRS Dana Amanah was established as an effort to support shared prosperity through the application of Islamic banking principles.

BPRS Dana Amanah is a growing and developing bank, so it has good prospects for investment or partnership in business. As the second BPRS established in Surakarta, the bank is located at Jl. K.H. Agus Salim No.18 Surakarta. Its strategic location makes it easy for people to access the services provided. Although BPRS Dana Amanah is newly operating, the community does not need to doubt the security

of their deposits, because this bank has been guaranteed by the government through the Deposit Insurance Corporation (LPS). With the motto "Spreading Sharia Reaping Barakah", BPRS Dana Amanah emphasises entrepreneurial spirit, mutual help, management excellence, and innovative investment orientation to maximise added value for stakeholders.<sup>48</sup>

The direct impact of the Covid-19 outbreak is inevitable, and various strategies are still being pursued to date, as the impact is still being felt by some customers. During the Covid-19 period, BPRS Dana Amanah was very grateful that financing for housing developers was not greatly affected by the pandemic. BPRS Dana Amanah's portfolio showed a positive development, with an increase from 2020 to 2021, and financing during the pandemic experienced a significant increase. BPRS Dana Amanah has also started to enter business sectors that were previously affected by Covid-19. The lodging sector is one of the most affected, with a decline to zero visitors, followed by the culinary sector. However, other sectors have shown signs of recovery. *The Sergu* product is one of the most popular products at BPRS Dana Amanah, and the Haji product is currently being reviewed for marketing and promotional development.

On the other hand, the business analysis and collateral provided remain competitive, although not yet focused on product development. BPRS Dana Amanah Surakarta has conducted MoUs with the real sector, which are still ongoing. However, since in the last one to two years it has not focused on the sector, BPRS will try to re-establish MoUs with some dealers. Nonetheless, data shows that the majority of dealers already have leasing cooperation, such as Honda with FIF. During the pandemic, the MSME sector continues to run albeit with reduced activity. BPRS Dana Amanah Surakarta has been marketing its products in this area for almost 8 years, with active efforts in exploring potential customers and good prospects. During the Covid-19 period, the bank tended to focus on schools, given that teachers were carrying out online learning. To attract interest, BPRS Dana Amanah Surakarta offers various promos, approaches the teachers' community, and conducts socialisation during meetings.

Innovations that have been pursued over the past six months during the pandemic include Hajj and Umrah products developed by management. This programme has started to attract many pilgrims. BPRS Dana Amanah Surakarta needs to have a strong mentality to ensure that sharia principles are applied, as implementation is not always easy. This is due to the complexity of the contracts, where a single transaction can involve up to three different contracts. Sharia schemes are still facing acceptance challenges among the public.

In early 2022, BPRS Dana Amanah began implementing the *real cost* concept as a substitute for administrative costs. This step is expected to increase efficiency to achieve the vision of BPRS Dana Amanah. The costs incurred prior to

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<sup>48</sup> Interview with Fajar, Employee of PT BPRS Dana Amanah Surakarta, Surakarta City, October 2023

this contract are more specific and *real cost*-based, including the cost of printing contracts, stamps, etc., thus emphasising BPRS Dana Amanah's commitment to sharia principles. What attracts the attention of BPRS Dana Amanah is that subsidised housing *developers* in Solo have survived, in contrast to those in Jakarta who have suffered many losses due to the impact of the Covid-19 pandemic. Through this role, BPRS Dana Amanah has been handling subsidised housing financing since 2021 and shows a rapid growth graph until 2022. Developers are willing to take the risk, especially since subsidised housing in Solo, although on the outskirts, is still easily accessible from the city centre.

The data we obtained shows that the highest percentage of customers came from the MSME sector, at 72.52%. Followed by the services sector at 10.48%, the agriculture sector at 0.19%, the livestock sector at 0.15%, the mining sector at 1.36%, and the industrial sector at 3.61%. In the construction sector, the percentage reached 51.20%, while the trade sector was 5.53%, and non-MFI customers were recorded at 27.59%.

### **3. BPRS Bumi Rinjani Kepanjen**

BPRS Bumi Rinjani was established in October 1992 and began operations on 16 November 1992. PT BPRS Bumi Rinjani in accordance with the conversion from conventional system to sharia system based on the Decree of the Minister of Law and Human Rights of the Republic of Indonesia Number C-07850 HT.01.04.TH.2006 dated 17 March 2006 concerning Approval of Amendments to the Company's Articles of Association. Furthermore, Bank Indonesia Letter Number 8/57/KEP.GBI/2006 dated 7 August 2006 related to the Granting of Permission for Conventional Business Activities to become Business activities based on Sharia principles of PT BPRS Bumi Rinjani Kepanjen, Malang. Thus, BPRS Bumi Rinjani officially operated based on sharia principles on 1 September 2006.

During the Covid-19 pandemic, BPRS Bumi Rinjani's customers were significantly impacted, so the bank focused on providing stimulus to ease monthly payment obligations. At the beginning of the pandemic, many businesses were halted due to PPKM and working hour restrictions imposed by the government. BPRS Bumi Rinjani followed government policy by easing the burden on customers who were affected, both directly and indirectly, such as workers who were laid off. Some customers even received instalment relief for six months due to business closures or restrictions on operating hours, especially for night-time traders. Intensive communication with customers is carried out to ensure they are not burdened with full obligations. Entering the second year of the pandemic, after the stimulus, BPRS Bumi Rinjani began to focus on supporting MSMEs, especially in the form of refinancing to revive affected businesses. In 2020, a lot of funds were spent only on consumption due to the decline in business activities. MSME financing at BPRS Bumi Rinjani reached 50%, with trade as the dominant sector. The cottage industry model has not fully recovered as people's purchasing power is still low. A shift has also occurred in the culinary sector, where traders are shifting from ready-to-eat food

to frozen food products, which require lower capital. BPRS Bumi Rinjani also pays attention to the agricultural sector, particularly sugarcane, which has proven to remain strong and unaffected by the pandemic.

The potential of BPRS Bumi Rinjani is more likely to be in the lower strata of society, where financing in the hundreds of millions is still rare. Meanwhile, other BPRSs focus more on large financing, such as property, which has been severely affected because it is not running as it did before the Covid-19 era. The concept of *mini micro* financing is still very much needed by the community. The strength of BPRS Bumi Rinjani lies in the customer database that includes many customers with small financing. BPRS Bumi Rinjani also encourages staff to visit customers' business premises if they happen to be in the area, to strengthen relationships and monitor the condition of customers' businesses. The impact of the pandemic in this area is similar to that in Yogyakarta, particularly on the lodging business sector which has been hit hard and has experienced a complete lack of income.

In 2021, government policies underwent some changes, so BPRS Bumi Rinjani again provided stimulus to customers. Towards the end of 2021, BPRS Bumi Rinjani began to witness economic movement and was optimistic that the market would recover in 2022, as it had before Covid-19. In early 2022, businesses that had resumed operations showed a significant increase in turnover. However, there is still one business sector that has not fully recovered and has only reached an operational level of above 50%.

BPRS Bumi Rinjani faces obstacles related to regulations and technological developments. Although BPRS Bumi Rinjani actually has the ability to adopt the technology, the implementation cannot be executed immediately due to strict regulations. Regulations from the banking authority encourage cooperation with *fintech* or commercial banks, but BPRS cannot do it independently. One of the main differences between BPRS and conventional banks lies in the clearing system. To overcome obstacles in payment, BPRS Bumi Rinjani can utilise conventional bank media, although the use of technology such as *mobile banking* is not yet allowed. Hopefully, in the future there will be an understanding to facilitate transactions and technology adoption for BPRS.

The strategy that can be built by BPRS Bumi Rinjani involves coordination with the Central Leadership Department (DPP) which specifically handles information technology. It is hoped that this step will help overcome the various obstacles mentioned earlier. In terms of Islamic interbank transactions, mortgages, and cashless services, in-depth studies are required. However, BPRS together with micro and MSME institutions are committed to building a solid ecosystem that is not easily shaken. Based on data from BPRS Formes Yogyakarta, MSME customers consist of 30 customers in the small category, 48 customers in the medium category, and 115 customers in the micro category, totalling 183 customers.

Based on data collected in May 2022, BPRS Bumi Rinjani recorded the number of micro business customers reaching 5,692 customers with financing values ranging from Rp 50,000,000 to Rp 300,000,000. Small businesses followed with 13

customers with financing values between Rp 300,000,000 and Rp 2,500,000,000. Meanwhile, there are no customers from the medium business category. This data shows that BPRS Bumi Rinjani has a strong focus on the micro business segment which is the backbone of the local economy, especially among the lower strata of society. This segment is the bank's priority in providing financial support due to the high level of demand, as well as the huge growth potential in the small business sector that often does not get financing from conventional financial institutions.

#### 4. BPRS Formes Yogyakarta

The journey of BPRS Formes began with the desire of Sleman community leaders to build the community's economy through professional sharia-based financial institutions. On 22 December 2008 Bank Indonesia issued a decision letter of Formes Business License No. 10/86/KEP.GB1/DpG/2008, which officially gave operational permission to PT BPRS Formes. The first opening of PT BPRS Formes was conducted on 19 January 2009, marked by a *soft opening* event.

BPRS Formes was established on the initiative of colleagues from Islamic microfinance institutions with the main objective of supporting the MSME sector. Therefore, BPRS Formes' portfolio is dominated by MSME financing which reaches 80%, in accordance with the bank's original mission of establishing the bank, which is to collaborate with figures who care about the development of MSMEs. BPRS Formes' service coverage focuses on MSMEs, while the remaining 20% is a synergy with other BPRS. Although BPRS Formes is not directly patronised by *stakeholders* to develop its role further, the institution remains committed to serving the micro sector. In terms of microfinance services, BPRS Formes competes with commercial banks and other financial institutions, such as pawnshops and cooperatives, which also contribute to supporting MSMEs.

BPRS Formes' personal approach has proven to be stronger than other institutions, which has enabled BPRS Formes to survive since 2009 with an initial capital of 1 billion rupiah. Currently turnover has reached 50 billion rupiah, as BPRS Formes strives to maintain capital and financial stability. Of the various sectors served, 80% of the portfolio is focused on the trade sector. In the education sector, there is a *multiplier effect* on the lodging sector, such as boarding houses and similar accommodation. The tourism and creative industry sectors were also affected, mainly due to the absence of face-to-face learning which resulted in low occupancy rates of boarding houses, which before the Covid-19 pandemic were heavily rented, resulting in a sharp decline in income in this sector.

Currently, the economy is starting to pick up again, although the biggest challenge occurred in March 2020, when the PPKM policy was implemented. At that time, access to villages or rural areas was closed, making it impossible to visit these areas. In the second wave, the number of cases was not as many as at the beginning of the pandemic, and now economic sectors are starting to move, including tourism which is back in operation. The education sector, although not fully recovered, is still

running with teaching and learning activities still conducted online. Gradually, people began to adapt to this change, and meetings can now be conducted virtually.

The role of BPRS in economic growth is greatly helped by policies issued by the authorities/regulators, for example in terms of increasing assets and productivity. In terms of income, BPRS is still in a sustainable condition, with no losses. In general, banks located in cities tend to experience a stronger impact than banks located in regencies. This may be due to mobility and other factors; for example, in Yogyakarta there is a *multiplier effect* coming from the education and tourism sectors. Meanwhile, the agriculture and trade sectors experienced high contraction in big cities such as Jakarta and Surabaya, while in Yogyakarta, Purwokerto, and Banyumas the contraction was less significant. There is a positive side to this situation, namely the emergence of creative ideas that encourage the development of new businesses to replace old businesses that are no longer operating.

Along with the times, especially in the era of digitalisation, BPRS Bumi Rinjani Kepanjen utilises social media for promotion and allows customers to apply for financing independently through *on the spot* services. This service is equipped with technology such as *mobile banking* to facilitate customers. In the validation process, BPRS Bumi Rinjani Kepanjen first checks the initial data from online forms such as Google Form, then proceeds to check the completeness of documents, including savings mutations. BPRS Bumi Rinjani Kepanjen also learnt from fintech in assessing partners based on the 5C components (Character, Capacity, Capital, Collateral, and Conditions). The main differences in the sharia system are related to the payment mechanism and character assessment. Minimum financing at BPRS Bumi Rinjani Kepanjen ranges from Rp 10,000,000 to Rp 1,200,000,000.

## 5. BPRS Metro Madani Lampung

BPRS Metro Madani is a financial institution that runs its operations based on Islamic sharia principles. PT BPRS Metro Madani commenced operations on 20 September 2005, was established based on the Deed of Articles of Association by Notary Hermazulia, SH, in Bandar Lampung No. 1 on 3 March 2005 and ratified by the Minister of Law and Human Rights with No. C-16872 HT.01.01.TH.2005 on 17 June 2005, and obtained a business license from Bank Indonesia with No. 7/54/KEP.GBI/2005 on 8 September 2005. Currently, PT BPRS Metro Madani has four branch offices and one Cash Service Office, namely the First Branch in Unit II Tulang Bawang (operating since 14 January 2008), Second Branch in Kalirejo District, Central Lampung Regency (since 1 November 2009), Third Branch in Daya Asri, Tumijajar District, West Tulang Bawang Regency (since 23 July 2012), Fourth Branch in Jatimulyo, South Lampung Regency (since 26 August 2013), and Cash Service Office at RSU Muhammadiyah Metro (operating since 15 October 2012).

At the beginning of the Covid-19 outbreak in March 2020, BPRS Metro Madani customers were still not significantly affected and remained calm. Conditions began to change when PPKM was enacted, which led to the suspension of Teaching and Learning Activities (KBM). The impact of the suspension greatly

affected the economy of Metro City, which is mostly engaged in the education sector. Arrears in instalment payments began to arise, initially one month, then two to three months, so anticipatory steps were needed to detect customers who were experiencing payment difficulties. BPRS Metro Madani then conducted a survey to understand the reasons for late payments and, if the customer was directly affected by Covid-19, offered a solution in the form of relaxation in accordance with OJK regulations. BPRS Metro Madani also identified some potential financing issues that may arise as a result of the pandemic. Of these customers, only a small number are eligible for relaxation, as the assessment is based on certain aspects that must be met, as was done in the initial financing application process.

The strategy applied by BPRS Metro Madani is product differentiation, given the challenges in marketing micro products that are quite difficult. Since September 2019, BPRS Metro Madani launched a Hajj bailout product which became the main focus of sales. In 2020, this product experienced a significant increase in sales, reaching its peak in 2021, before levelling off again in 2022. This decline is considered reasonable, given the market conditions that have begun to shift to the business sector. In addition, the two-year delay in Hajj departures caused potential customers to rethink their applications. However, once Hajj departures return to normal, an increase in demand is expected. This Hajj bailout product has proven to help stabilise revenue and achieve the set target.

On the other hand, there are external constraints, especially for MSMEs related to collateral, which makes some potential customers consider the option of moneylenders who do not require collateral. After consulting with BPRS, potential customers are often constrained by the collateral aspect. Microfinance at BPRS Metro Madani starts from Rp 5,000,000, but for the super micro product there are many requirements that make it less attractive to customers. Other constraints, both internal and external, relate to insurance coverage which is still difficult to access, with many insurers withdrawing from co-operation.

BPRS Metro Madani has taken policies to increase outstanding, one of which is through gold pawning products. This product is not only used for consumption, but also as business capital and is experiencing increased demand. There are no regulatory constraints from the government related to this product. For financing, BPRS Metro Madani uses murabahah and mudharabah contracts. Previously, the bank worked with cooperatives, but the cooperation was shifted to mudharabah and partly to musyarakah. Ijarah is only used in certain cases, while the latest product offered is Musyarakah Mutanaqisah (MMQ), which is designed to respond to the closure of the relaxation programme from March 2022. In case of future problems, and the situation improves, BPRS Metro Madani sets special requirements in the form of collateral, such as land assets, houses, or vehicles in the name of the spouse. BPRS Metro Madani will purchase according to the current outstanding, so that the purchase portion is only partial, while the seller retains a certain portion.

Data collected from BPRS Metro Madani shows that there are 189 productive MSME customers utilising financing for working capital, with total outstanding

financing of IDR 8,550,455,488. These customers cover a wide range of small and medium enterprise sectors, which play an important role in supporting the local economy and creating jobs. This working capital financing is provided to help MSMEs increase production capacity, expand business, and strengthen competitiveness amid economic challenges. With BPRS Metro Madani's commitment to supporting the MSME sector, it is hoped that this financing can encourage more sustainable local economic growth and improve the welfare of the communities around its operational areas.

### **Findings on the Transformation of the Strategic Role of BPRS in Improving the National Economy in the Pandemic Era and Future Challenges**

Referring to the various theoretical concepts and field data presented above, it appears that the transformation of the strategic role of BPRS in improving the national economy is very relevant in relation to the theory of economic growth that highlights the importance of investment, productivity, innovation, and equitable distribution of public welfare. In the context of classical economic growth theory, Adam Smith emphasised that growth can be achieved through an efficient division of labour to increase productivity and wealth distribution.<sup>49</sup> The role of BPRS in supporting the MSME sector is significant, especially by providing access to affordable financing for small businesses that contribute to increasing the scale of production, creating jobs, and improving community welfare. In the long run, these efforts strengthen the local economy which cumulatively supports national economic growth.

According to modern economic growth theories, such as the Harrod-Domar model, investment is a key factor in increasing production capacity.<sup>50</sup> BPRS in Indonesia serves as an investment catalyst for MSMEs through profitsharing-based Islamic financing, such as *mudharabah* and *musyarakah*, which provides convenience for MSMEs without burdening them with interest. With this access to capital, MSMEs can increase their production capacity and economic output, making a positive contribution to the local and national economy. This strategy also reduces the excess risk that is commonly present in conventional credit schemes, making BPRS a financial institution that supports economic stability.

In addition, Paul Romer's endogenous growth theory states that innovation and human capital improvements are the main drivers of long-term growth.<sup>51</sup> BPRS is transforming by adopting digital technology that enables them to reach more customers in remote areas and improve efficiency. These innovations not only facilitate customer access to financial services, but also strengthen the competitiveness of BPRS against conventional banks and nonbank financial

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<sup>49</sup> Smith, *An Inquiry Into the Nature and Causes of the Wealth of Nations*.

<sup>50</sup> Jody Gordon, *Economic Development in Rural Sector* (United Kingdom: Scientific e-Resources, 2019), p. 109; See also R. Ramanathan, *Introduction to the Theory of Economic Growth* (Berlin Heidelberg New York: Springer Science & Business Media, 2012), p. 18.

<sup>51</sup> Tom G Palmer, *And Economic*, n.d.

institutions such as fintech. On the other hand, BPRS plays a role in human capital development by providing financial education to MSME customers, which encourages better financial management and productive business practices. This is in line with the principle of endogenous growth that focuses on human capital and innovation as the main pillars of sustainable growth.

The role of BPRS in creating inclusive economic growth is also related to structural economic growth theory which emphasises the importance of equitable development. As an Islamic bank, BPRS is orientated towards the principles of justice and shared prosperity, and targets economic sectors that are often overlooked by conventional banks, such as MSMEs in remote areas. In doing so, BPRS helps to create financial inclusion, which is important to ensure that economic growth can be felt by all levels of society.

The transformation of BPRS' strategic role in the digital and pandemic era is also relevant to Schumpeterian growth theory, which emphasises innovation and technological change as the main drivers of growth. According to Schumpeter, innovative financial institutions will trigger a new wave of growth. By adopting digital technology and working with fintech, BPRS is capitalising on this momentum to improve efficiency, reach new customers, and provide more responsive services. This innovation allows BPRS to play a bigger role in supporting the growth of MSMEs, especially in areas that have not been touched by conventional banking services.

Going forward, BPRS can continue to transform by applying various aspects of growth theory, such as strengthening digital capacity, expanding financial education to improve human capital, and creating innovative sharia products. By combining sharia principles and modern economic growth theory, BPRS not only functions as a financial institution, but also as an agent of sustainable economic development. This transformation enables BPRS to remain relevant and contribute significantly to national economic growth, realising an inclusive, equitable and sustainable Islamic economy.

This reflects a shift in the strategic role of BPRS—from merely financial intermediaries to agents of inclusive economic development—requiring reform in legal frameworks, digital adaptation, and stronger institutional alignment. The findings imply the need for regulators such as OJK and regional policymakers to develop integrated legal frameworks that are more responsive to the needs of MSMEs during crisis recovery. BPRS must also be supported to adopt digital platforms and enhance legal risk management to ensure compliance and sustainability. While Beck et al<sup>52</sup> highlighted the regulatory rigidity of Islamic banks in crisis contexts, this study finds that BPRS in Indonesia, when equipped with flexible, localized regulatory support, can effectively support MSME resilience even

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<sup>52</sup> Thorsten Beck, Asli Demirgüç-Kunt, and Ouarda Merrouche, "Islamic vs. Conventional Banking: Business Model, Efficiency and Stability," *Journal of Banking and Finance* 37, no. 2 (2013), p. 433–47.

during national downturns. This study contributes to the literature by exploring the regulatory and strategic transformation of BPRS in a post-pandemic setting, a dimension rarely discussed in previous research, which mostly focuses on commercial Islamic banks or financial performance alone.

## Conclusions

The results of this study show that the strategic role of Sharia People's Financing Banks (BPRS) in supporting Indonesia's economic growth is realized through the performance improvement and distribution of business capital to Micro, Small and Medium Enterprises (MSMEs). With increased capital distribution, BPRS contributes to job creation, as MSMEs supported by financing are able to absorb more workers. This finding aligns with classical growth theory (Adam Smith), which emphasizes productivity and employment in the small business sector as essential components of national economic growth. BPRS applies the precautionary principle in financing management, acknowledging the relatively high-risk nature of the MSME sector. By maintaining sound financial health and complying with applicable regulations, BPRS is able to remain sustainable while targeting the grassroots economy. Despite its small scale, BPRS's reach is wide and impactful, contributing to increased MSME independence and resilience. Since the Covid-19 pandemic, BPRS has allocated an average of 68.25% of its total financing to the MSME sector, helping stimulate local production, expand employment, and strengthen national income. These findings also support endogenous growth theory, which emphasizes the importance of human capacity development and economic self-reliance for long-term, sustainable growth. The implication of this research is that BPRS must be supported through a more adaptive legal and regulatory framework especially to meet the real financing needs of MSMEs during times of crisis and economic recovery. Regulators such as the Financial Services Authority (OJK) and regional governments must collaborate in developing inclusive legal instruments that empower BPRS to transform from traditional micro-lenders into strategic agents of inclusive economic development. This includes strengthening legal protection for micro-entrepreneurs, promoting digital adoption in BPRS operations, and encouraging integration with national and local economic development programs. Through such efforts, BPRS can fulfill its dual mandate complying with sharia principles while actively contributing to equitable and sustainable national economic growth.

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## Interviews

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