

# The role of microfinance institutions in eradicating poverty in fishmonger communities in Makassar, Indonesia

## El papel de las instituciones microfinancieras en la erradicación de la pobreza en las comunidades de pescadores en Makassar, Indonesia

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### Abstract

This study aimed to analyze the relation among microfinance institutions, small and micro enterprises, competitiveness, social capital, and poverty eradication using partial least square analysis. The analysis unit was 100 fishmongers who use money from microfinance institutions and work in the Paotere fish market in Makassar, Indonesia. Microfinance institutions influences the competitiveness of fishmongers, strengthens their social capital, and eradicates poverty around them. The managers of microfinance institutions should maintain their cooperation with fishmongers to ensure that the loans they give don't only benefit the borrowers.

**key words:** fishmonger, microfinance institution, poverty, social capital

### Resumen

Este estudio tuvo como objetivo estudiar la relación entre las instituciones de microfinanzas, las micro y pequeñas empresas, la competitividad, el capital social y la erradicación de la pobreza mediante el análisis parcial de mínimos cuadrados. La unidad de análisis fue de 100 pescaderos que utilizan dinero de instituciones de microfinanzas y trabajan en el mercado de pescado Paotere en Makassar, Indonesia. Las instituciones microfinancieras influyen en la competitividad de los pescaderos, fortalecen su capital social y erradican la pobreza a su alrededor. Los gerentes de las instituciones de microfinanzas deben mantener su cooperación con los pescaderos para garantizar que los préstamos que otorgan no solo beneficien a los prestatarios.

**Palabras clave:** pescador, institución de microfinanzas, pobreza, capital social

## 1. Introduction

Microfinance institutions provide a strategic role in the provision of financial services, especially for low-income communities and small and micro entrepreneurs. Bappenas (National Development Planning Agency of the Republic of Indonesia) reported in 2011 that the number of microfinance institutions in Indonesia had reached

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94000 units, placing Indonesia as the country with the highest number of microfinance institutions in the world during the last 25 years. However, these institutions are still hampered by various problems such as diversified institutionalization, limitations in their capacity to collect and distribute funds, and low managerial skill levels. Despite the growth of microfinance institutions, Indonesia is still faced with the problem of high level poverty. Based on the data from Indonesian Central Bureau of Statistics, the number of persons in poverty in 2014 reached 27.73 million, 10.96 percent of the total population, mostly working in the sectors of agriculture and fishing, sectors normally excluded from access to banking institutions. Fishing communities generally face problems of low education, low marine knowledge, limited capital, and low business managerial skill. In particular, fishmongers, as a part of coastal communities, have lower education and social economic levels than non-coastal communities, so they tend to remain in poverty and underdeveloped (Karyani, 2012). Thus, microfinance institutions are still needed to fund businesses in the fishery sector. Sebstad (1998), Woller, Dunford, and Woodworth (1999), and Robinson (2001) have shown that microfinance institutions can play a role in eradicating poverty by increasing the consumption and income of poor families.

Most micro and small business still rely on self-sourced capital, which makes their business remain in an under-capacity condition. In addition, problems of bank ability, collateral principle, and procedural complexity are factors that make access to loans difficult for poor people. Therefore, the role of social capital has become an important factor in establishing relationships between microfinance institutions and poor communities. It is also frequently found that the relationship pattern between creditor and debtor is a patron-client relationship (Wakarmamu, 2010), and it can become a catalyst for poor communities (Ariana, Kusbiantoor, & Setiawan, 2006).

The paotere fish market, is a place where fish are sold through auction, is a location in the city of Makassar (Indonesia) used by fishmongers to sell their wares. Many have difficulties in obtaining business capital and accessing banking institutions. Some of them depend on certain microfinance institutions and informal financial institutions such as *punggawa* (a local term for moneylenders) that offer loans with high-interest rates (Wakarmamu, 2010). This phenomenon is believed to influence business competitiveness and even increase poverty in the community.

This study analyzes the relation between microfinance institutions, micro and small enterprises, social capital, competitiveness, and poverty, especially its eradication, in the fishmonger community in the Paotere fish market in the city of Makassar, South Sulawesi, Indonesia.

### **1.1. Microfinance institution and poverty eradication**

The position of microfinance institutions in the financial system is as an intermediary between banks (formal sector) and the informal sector. It is called microfinance because its clients operate at a small scale (despite the fact that this group of clients is the majority of the population). This institution can also be a social mediator, facilitating group establishment, confidence development, and management and financial training within the newly formed groups. Rock, Otero, and Saltzman (1998) have explained that microfinance institutions combine a social and commercial mission.

Microfinance institutions can be Non Governmental Organizations (NGO's) savings and loan cooperatives, government banks, commercial banks, or non-bank financial institutions. Their clients are characteristically entrepreneurs with low incomes located in both cities and villages. They are merchants, peddlers, farmers, and service providers such as barbers, craftsmen, blacksmiths, and tailors, whose activities are producing a source (or sources) of stable income yet remain vulnerable to poverty.

In their decision making, microfinance institutions must consider two long-term objectives: outreach and sustainability. Outreach means serving those who are not handled by formal financial institutions, and sustainability is the institution's ability to survive by collecting adequate income to cover its operational

expenses. In its effort to anticipate poverty and empower small businesses, microfinance institutions are grouped into two types according to their approach: (a) an institutional approach or (b) a welfare approach (Robinson, 2001). Several studies have focused on the role of microfinance institutions in eradicating poverty, and have generally seen them have positive results (Sebstad, 1998). Microfinance institutions increase financial sustainability, which is achievable together with poverty counter measures. In this approach, sustainable effort to reduce poverty can be achieved by using a double strategy, increasing the productivity of the poor and providing basic social services for them. Microfinance institutions are believed to be instrumental in increasing the productivity of the poor by focusing its attention on the failure of credit market to serve this population and by maximizing market opportunities. More than just providing financial services for micro businesses and poor families, it is a holistic strategy to decrease poverty level using several different methods.

## 1.2. Social capital and competitiveness

There are many definitions of social capital. According to Adler and Seok (2002), social capital is an ambiguous concept with multiple definitions. Ancok (2003) has grouped definitions of social capital into two large groups. The first group emphasizes social networks bound by information ownership, trust, mutual understanding, value similarity, and mutual support, while the second emphasizes traits embedded in individuals involved in a social interaction (Adler & Seok, 2002). Coleman (2014) developed social capital theory in the late 1980s by observing the functional perspective of social capital. He noted that social capital was not a singular entity but a plural and varied entity that consists of a social structure that facilitates the conduct of certain actors in the structure. This definition is supported by Putnam (1993), who has mentioned that social capital refers to civil norms and networks that reinforce cooperation among citizens and their institutions. Putnam (1993) asserted that social capital is related to social organizations, social bonds or relationships, norms, and trust that facilitates coordination and cooperation for mutual benefit.

Rahmana (2009) has defined competitiveness as the ability to maintain market share, which is determined by competitive price. Both factors can be achieved by having and using the ability to innovate. Competitiveness influences productivity improvement and market access expansion, which leads to increases in sales turnover and business profitability.

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## 2. Methodology

This explanatory study uses a positivist approach and focuses on fishmongers who are using loans from microfinance institutions located around the Paotere fish market in the city of Makassar, South Sulawesi, Indonesia. Using purposive sampling: 100 fishmongers were selected as the sample for this study. This study analyzed the relationship among microfinance institutions ( $X_1$ ), competitiveness ( $Y_1$ ), social capital ( $Y_2$ ), micro and small enterprises ( $Y_3$ ), and poverty ( $Y_4$ ). Microfinance institutions are the exogenous variable, while competitiveness, social capital, micro and small institutions, and poverty are endogenous variables. The measurement of the research variable used a Likert scale to observe the attitude, opinion, and the perception of respondents toward the research object (Nasir, 2009). The Structural Equation Model/SEM-PLS was used to analyze the relations among variables (Nasir M. 2009).

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## 3. Results

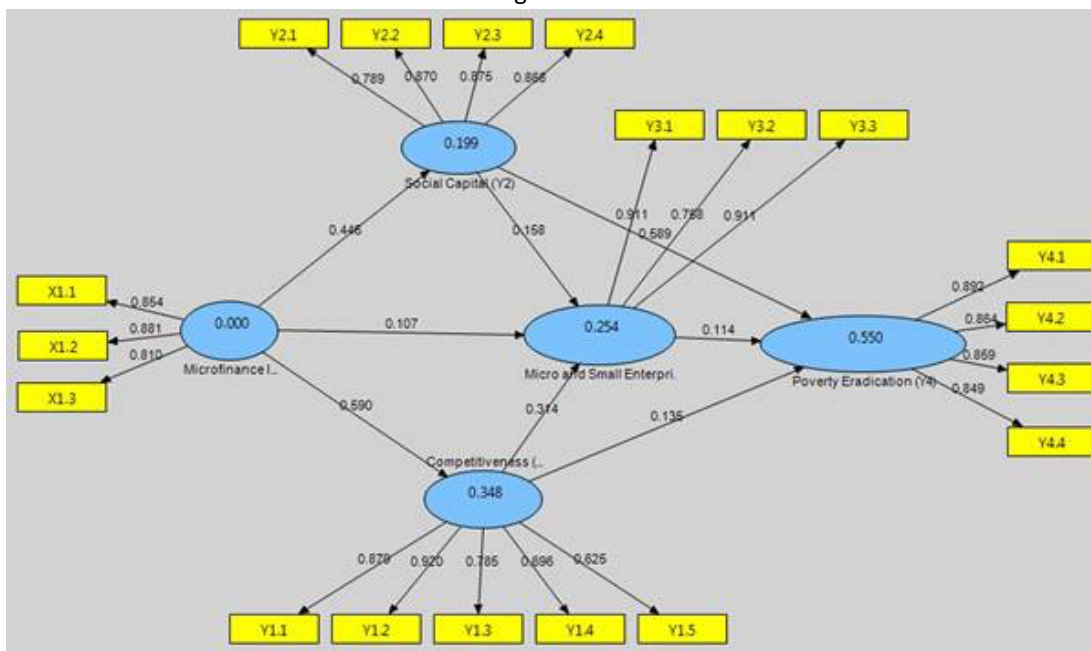
Path analysis on the relation among the variables in the Structural Equation Model/SEM-PLS produces two assessment results, the outer model and inner model. The former is the relation path between the research variables and their indicators. The result of the outer model assessment is described by comparing the outer loading value and mean of respondent's assessment on each indicator of the research variables. The inner model assessment is known as a goodness-of-fit model in the form of predictive relevance value ( $Q^2$ ), which is the value

that explains the magnitude of predictive relevance over the model being constructed, thus determining the worthiness of hypothesis testing.

### 3.1. Result of outer model test

The variable of this study is a reflective indicator, which is a quantitative measurement of the perception of fishmongers who use Micro Financial Institution (MFI's) fund. The highest outer loading value is defined as the most appropriate indicator for describing the variable in question. Based on the result of MFI variable measurement, the outer loading value of loan level is the highest, which means that the aforementioned indicator has the highest capacity to describe the MFI variable. Fishmongers largely agreed that the amounts of the loans received by fishmongers are detrimental to their usage of MFI's fund in supporting their business. The result of competitiveness variable measurement shows that capital is the most appropriate indicator for describing the competitiveness variable. Fishmongers agree that capital is an important factor in determining the competitiveness of their business. It means that this value is a signal that, in order to improve business competitiveness, Micro Small Enterprises (MSE) particular fishmongers, need to increase their capital. The result of the social capital variable shows that cooperation has the highest outer loading value, which means that cooperation is the best indicator for describing the social capital variable. Cooperation is the most important factor in creating social capital for fishmongers to interact with MFIs. The cooperation aspect is emphasized on togetherness values between fishmongers and MFIs. It promotes dialogue in solving problems and enables feedback and sharing of information regarding the development of fishmongers' business and honesty value embedded in the cooperation. The result of SME variable measurement shows that loan appropriateness has the highest outer loading value, meaning that the balance between the amount of loan and fishmongers' income is an important aspect in determining the condition of their business. The result of poverty eradication variable shows that income has the highest outer loading value, suggesting that fishmongers' income is an important aspect in determining their poverty. The output of the analysis of the relationship between MFIs, competitiveness, social capital, SMEs and poverty eradication using the Partial Least Square (PLS) method is showed in Figure 1.

**Figure 1**  
The testing model research



### 3.2. Result of the inner model test

In PLS analysis, the inner model test is known as goodness-of-fit model stated in predictive *relevance* ( $Q^2$ ) value, which is a value that explains the predictive power over the model being constructed, so it determines fitness in hypothesis testing (Table 1). A value of  $Q^2 > 0$  shows that the model has predictive relevance, while a value of  $Q^2 \leq 0$  shows that the model does not have adequate predictive relevance (Ghozali & Latan, 2015). The result of the inner model test in this study showed a  $Q^2$  value of 0.8250, so the model had predictive relevance for hypothesis testing. The following is the result of PLS-based research model testing using SmartPLS 3.0 (Ghozali & Latan, 2015).

**Table 1**  
Result of research model testing

Relation between variables		Path coefficient	T- statistics*	p-value*	Remark
MFI (X <sub>1</sub> )	Competitiveness (Y <sub>1</sub> )	0.590	14.688	0.000	Significant
MFI (X <sub>1</sub> )	Social Capital (Y <sub>2</sub> )	0.446	8.861	0.000	Significant
MFI (X <sub>1</sub> )	MSE (Y <sub>3</sub> )	0.107	1.150	0.250	Insignificant
Competitiveness (Y <sub>1</sub> )	MSE (Y <sub>3</sub> )	0.314	3.216	0.001	Significant
Competitiveness (Y <sub>1</sub> )	Poverty Eradication (Y <sub>4</sub> )	0.135	1.517	0.129	Insignificant
Social Capital (Y <sub>2</sub> )	MSE (Y <sub>3</sub> )	0.158	2.248	0.025	Significant
Social Capital (Y <sub>2</sub> )	Poverty Eradication (Y <sub>4</sub> )	0.589	7.359	0.000	Significant
MSE (Y <sub>3</sub> )	Poverty Eradication (Y <sub>4</sub> )	0.114	2.140	0.032	Significant

\*Hypothesis testing criteria: significant if t-statistic > 1.960 or p value < 0.05 (Ghozali and Latan, 2015).

### 3.3. The influence of MFI on competitiveness

This finding shows that the level of loans from MFI received by fishmongers was the factor that had the biggest influence on the competitiveness of fishmongers in running their business. The loans they got were used to add to the capital they had from sales made, so they had the confidence to increase the kind and the number of fish they sold. In addition, using the funds they receive from MFI, they had a willingness to use technology that can support their business.

This finding supports the results of Woller et al. (1999) and Robinson (2001), which revealed that loans obtained from financial institutions can help clients develop their business without sacrificing installment level and institutional sustainability. MFIs, whose benefit is enjoyed by fishmongers in Paoterefish market, are financial institutions emphasizing on welfare approach (Rock et al., 1998) because the existence of those MFIs is not only for profit but also for client coverage (such that service users can obtain more benefit from the existence of the MFIs).

### 3.4. The influence of MFI on Social capital

This finding shows that the choice of MFI made by fishmongers has a significant influence on the emergence of social capital in forms of trust, norms, cooperation, and communication. The use of loans from certain MFIs and the frequency of fishmongers in applying for loans strengthen the fact that fishmongers and MFI managers have built a good cooperative relationship. Furthermore, the choice of MFI type and borrowing frequency indicates that mutual trust exists between them and that communication between them has gotten better. In addition,

the decision of fishmongers to use loans from MFIs is a reflection that they are willing to obey and comply with norms and rules that regulate the cooperative relationship between them. Thus, the use of loans from MFIs does not only add to the business capital of fishmongers but also strengthens their social capital.

Empirical facts obtained from this research show that the close relationship between fishmongers and MFI administrators has been active and persistent, in which the cooperation is bound by values of honesty, mutual trust, and mutual understanding. This finding supports Brehm and Rahn (1997), who stated that cooperation within and among communities created social capital due to mutual understanding, value similarity, and mutual support. Cooperation is a strong indicator in describing social capital between fishmongers and MFI administrator, as revealed in this research. The findings of this research also confirm Cohen and Prusak (2001), who stated that social capital is created from active relationships among individuals or organizations that bind the parties in a network and enable cooperation among them.

### **3.5. The influence of MFI on MSE**

Empirical facts obtained from this research show that the amount of loan, borrowing frequency and decision on types of MFI for loan application do not directly influence the business condition of fishmongers, nor do they increase their business turnover. This is because of the fact that even though fishmongers decided the type of MFI they chose for their partner, the loan they get is used not only for business capital but also for the fulfillment of their household consumption such as for the needs of their children. This applied to all fishmonger families. The cause of this condition can be observed from two sides. From the perspective of the debtor, easier loan applications and more lenient installments make them “dare” to apply for loans whose objective is not for business development. From the perspective of creditors, the principle of loan granting does not focus on the purpose of the loan, so MFIs do not have “room” to limit the use of the loan. They only limit the amount and the repayment period of the loan. However, there are still fishmongers who are faced with an imbalance between the amount of the money they borrow and their income level, so the loan becomes a business expense. The amount of loan they get does not directly affect their business turnover and business improvement. This condition usually applies to fishmongers who borrow money from *punggawa*, individuals who lend money for high-interest rates. They bind their borrowers, such that they are highly dependent on them.

This finding contradicts the finding of Karay (2012), who revealed that loan procurement and management by micro and small entrepreneurs significantly influence the empowerment and improvement of their business. Similarly, Hermes, Lensink, and Meesters (2011) revealed that loans distributed to poor people in developing countries improved their socioeconomic conditions.

### **3.6. The influence of competitiveness on MSE**

The finding of this study asserts that competitiveness plays an important role in improving business conditions, business turnover, and ability to repay the loan. Competitiveness is measured from dimensions of business capital, fishmongers' skill, ability to master technology, and ability to access information particularly related to business development.

Fishmongers with adequate business capital tend to have the ability to develop their business, increase sales volume, and improve their chances to expand their market. Therefore, their business will be better and turnover larger. In the aspect of technological mastery and information access, fishmongers who use communication technology such as mobile phones tend to have the ability to establish communication with MFI administrators regarding the condition of their business and their loan repayments. In addition, they can build communication with their customers regarding the fish they sell (market share expansion). Mastery in fish processing technology,

which is a form of business diversifications, increases business turnover and even helps fishmongers reduce loan expenses.

This finding supports the result of Rahmana (2009), who explained that competitiveness influenced productivity and expanded market access. Furthermore, competitiveness encourages fishmongers to adapt to consumer preferences and to differentiate products they sell, which eventually increases their sales turnover and business profitability.

### **3.7. The influence of social capital on MSE**

The result of this research shows that social capital has a direct influence on Micro Small Enterprises (MSE). Social capital between fishmongers and MFI plays an important role in improving business, increasing business turnover, and increasing the ability of fishmongers to repay the loan. This finding is supported by the result of interviews on several fishmongers, who revealed that cooperation between themselves and the MFIs was built on mutual trust, honesty, mutual understanding, compliance with the agreed-to contract, and high fellowship values. Fishmongers hold the cultural value of *siri*, a local word for “ashamed,” in their relations with MFI administrators. They are ashamed if they do not do what they say if they do not comply with their contract and if they are not honest about the condition of their business or their income. They are even ashamed of having debt. It is believed that the application of this cultural value strengthens social capital, making trading business in Paotere sustainable for generations.

This finding supports the empirical study of Wakarmamu (2010), who stated that the relationship pattern between creditor and debtor was similar to the relationship of patron-client, so the relationship that created the social capital influenced probability and output. Furthermore, this finding confirms the findings of Paldam and Svendsen (1998) in Chuzu (2002), who included social capital into the production factor, just as classic economics includes human resources into the production factor, and concluded that social capital influenced business output. This finding also confirms Ariana et al. (2006), who stated that social capital was a catalyst for poor communities (small and medium business people) to access loans from MFIs. Thus, this finding is a signal that social capital in forms of trust, norms, cooperation, and communication needs to get the attention of business people since it can extend access for capital loans, improve business conditions, and help to determine the income derived from the business.

### **3.8. The influence of competitiveness on poverty eradication**

The empirical facts of this research showed that, in general, the condition of business capital owned by fishmongers was the most important indicator in determining their competitiveness. However, the analysis of the influence of competitiveness on poverty eradication concluded that business capital (which is mostly borrowed money) did not influence poverty in the fishmonger community. This indicates that there are other factors that make business capital ownership not directly correlate with fishmonger’s income level. It was frequently found that fishmongers own some capital (borrowed from MFIs) but the money is not allocated directly to business development. Factors limiting financial management and careless financial planning were the reason behind the failure of fishmongers to increase their income, hindering them from getting out of poverty.

This finding is supported by the result of interviews with several fishmongers, who revealed in general that they had limitations in managing and regulating the use of loans, in acquiring information related to business development, and in mastering technology that supports their business. In addition, they frequently felt awkward and not confident in involving themselves in meetings with fellow fishmonger groups or with MFI administrators to share knowledge regarding business management. This affected their ability to improve their

competitiveness. It meant that they were facing a condition where their business and socioeconomic life cannot change for the better.

### **3.9. The influence of social capital on poverty eradication**

The findings of this study show that the relationship between social capital and fishmongers on the basis of trust, norms, cooperation, and communication were able to eradicate poverty in fishmonger community directly. The empirical facts showed that, according to fishmongers, cooperation is the most important dimension in determining social capital, which creates relationships between fishmongers and MFIs. Furthermore, aspects of trust, norms, and communication are important components that create social capital in the relationship between fishmongers and MFI managers. Trust is positioned as the main principle for fishmongers in applying for loans because they assume that debt is not merely a trust given to the debtor, but it also a form of *siri* test. For fishmongers (who generally belong to Bugis tribe in Makassar), *siri* is a cultural heritage that must not be compromised for material objects. Therefore, fishmongers who borrow money from MFIs are ashamed if they have debt, ashamed if they lose the trust for another loan, and, consequently, ashamed if they cannot keep their word and break the contract they have made with MFIs. The application of *siri* strengthens the relation of social capital between fishmongers and MFI managers, improves the communication between them, and reduces transaction cost in getting a loan. The implication of the combination between cultural values and social capital is that fishmongers have a strong motivation to earn income, so they can get out of poverty.

This finding supports the empirical study of Collier (1998), who stated that cooperation and knowledge sharing reduced opportunistic behavior and transaction cost. As in Wilson (2000), Rauch (2001), and Schideler (2005), in the aspect of microfinancing, social capital improves information sharing, reduces transaction cost, and reduces other forms of uncertainty. Therefore, it is important to maintain those factors to reduce poverty in fishmongers who use a loan from MFIs.

### **3.10. The influence of MSE on poverty eradication**

The result of this study shows that MSE influences poverty eradication in the fishmonger community. The empirical facts show that conformity between income and loan amount, according to fishmongers, is the most important dimension in describing the condition of business development. Fishmongers are faced with problems of limited capital, so they are in need of loan to improve their businesses. Thus, conformity between the ability to repay the loan and the income they have is important to consider. It means that, just in case of imbalance, fishmongers in question tended to have difficulties in repaying their debt, which eventually worsened their condition.

In addition, business conditions and turnover were also determiners of their business sustainability. The properties of their chief commodity, which is perishable and relatively homogenous (relatively similar to the commodities of other sellers), make fishmongers have a high dependency on their (regular) customers. They do not have the power to set the price of the fish, so it is difficult for them to estimate the turnover they may get. The facts showed that the income from and expenses of their business are relatively predictable, even though the profit they get is relatively low. Therefore, business conditions and turnover of fishmongers significantly influence their income and expenses.

Some fishmongers admitted that their business, in spite of the fact that they still count on the loans from MFIs, indicating that the business is still under capacity, has lasted for a long time and has helped them get out of poverty. Thus, the empirical facts found in this study assert that fish-selling business is able to eradicate poverty in fishmonger communities, especially in the Paotere fish market. Therefore, the aspect of MSE has an important role in eradicating poverty of fishmongers who use loans from MFIs.



This finding supports the empirical study of Woller et al. (1999), who found that MSEs helped build the economic capacity of poor families, reduced poverty and unemployment (Prasetyo, 2008), become an employment provider (Darwanto, 2011), enabled poor families to increase their consumption and manage their risk well (Durrani, Usman, Malik, & Ahmad, 2011). Therefore, a business run by fishmongers, as one type of SMEs, has played its role in eradicating poverty through improvement of income level and reduction of household expenses and has been influential for social welfare.

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#### 4. Conclusions

The presence of MFIs helped improve the competitiveness of fishmongers. The relationship between them had lasted for a long time and was built on social capital in forms of cooperation, mutual trust, honesty, and conformity to the agreement, and was able to improve their business conditions and turnover as well as the ability of the fishmongers in returning the loan they have received. However, cooperative relationships through loan attainment did not directly influence poverty eradication efforts. The attainment of business capital that mostly loans was not able to increase the income of fishmongers. The capital obtained by fishmongers was frequently not allocated directly to the development of their business. Managers of MFIs need to improve cooperation by providing accompanying services to ensure that the loan they provide is not only beneficial to debtors (welfare approach) but also beneficial to them in forms of profit and business sustainability (institutional approach). Furthermore, fishmongers need to maintain the social capital they have, especially trust, cooperation, and honesty, in order feasibly obtain low-interest and lenient loans from MFIs.

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