

Literature Study: Comparison of Traditional Banking Services and Fintech in Providing Access to Financing for MSMEs

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Abstract

MSMEs still face major obstacles in accessing financing, which is a major factor in supporting their growth and development. The availability of easy and fast access to financing is one of the main keys to advancing the MSME sector, but until now, this access has not been optimal. This study aims to compare the effectiveness of traditional banking and fintech services in providing access to financing for MSMEs. This study uses a qualitative approach with a literature study method. The data used comes from scientific journal articles, OJK and banking publications, news, online articles from credible sources. The data collected was then analyzed using a comparative analysis method between traditional banking and fintech services. The results of the study show that fintech and traditional banking services have their respective advantages and disadvantages in providing access to financing for MSMEs. Fintech excels in speed, inclusiveness, and technological innovation, while conventional banks are stronger in terms of regulation and security. The combination of these two approaches is very important to expand access to financing for MSMEs nationally.

Keywords: Fintech; Financing; Banking; MSME.

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INTRODUCTION

Micro, Small, and Medium Enterprises (MSMEs) play a vital role in Indonesia's economy. MSMEs contribute more than 60% to the Gross Domestic Product (GDP) and employ over 97% of the workforce (Central Statistics Agency, 2022). However, many MSMEs still face challenges in accessing adequate financing from financial institutions. Yet, access to financing is a key factor in developing MSMEs that significantly contribute to economic growth and job creation. The availability of easy and quick access to financing is one of the main keys to advancing the MSME sector, but to date, such access remains suboptimal.

Traditional financial institutions such as banks are typically the primary choice for MSMEs seeking financing. However, many SMEs are hindered by complex procedures, strict requirements, and high interest rates (Suryani, 2021). According to Supeni et al. (2022), strict loan criteria, lengthy and complex administrative processes, and collateral requirements exceeding the financial capacity of small businesses make it difficult for many SMEs to obtain sufficient funding.

On the other hand, the emergence of financial technology (fintech) offers more flexible and faster solutions in providing financing services. According to Alperovych et al. (2022), fintech provides more flexible alternative financing solutions that are easier to access compared to traditional financing. Fintech enables SMEs to access financial services through

simpler processes and shorter timeframes. With simpler processes and less stringent requirements than banks, small businesses can optimise their income through quick access to capital. This enables them to capitalise on growth opportunities, manage unexpected cash flows, and maintain operational sustainability (Utami, A. N. B., et al., 2024).

However, fintech also faces challenges related to regulation, data security, and potential risks that may arise for users (OJK, 2023). According to Azizaj (2020), although fintech offers many advantages, its growth also presents certain challenges and risks, such as incomplete regulations, higher credit risks, and trust issues, which are some of the issues that need to be addressed. Therefore, the role of regulators is crucial in creating regulations that support innovation while protecting consumers and promoting the adoption of best practices in the industry (Utami, A. N. B., et al., 2024).

This study aims to compare the effectiveness of traditional banking services and fintech in providing access to financing for SMEs. By analysing the advantages and disadvantages of both types of services, it is hoped that a clearer picture will emerge of how these two sectors contribute to the empowerment of MSMEs. Additionally, this study is expected to provide policy recommendations to improve access to financing for MSMEs in Indonesia, develop more inclusive services, and identify potential collaborations between traditional banks and fintech in supporting the MSME sector in Indonesia, which will ultimately drive national economic growth.

The urgency of this research lies in the need to provide deeper insights into the effectiveness and potential of both financing service models (traditional banking and fintech) in improving financial access for MSMEs. Although topics related to fintech, traditional banking, and access to financing for MSMEs have been widely discussed, research that specifically compares the two service models in the Indonesian context is still limited. Therefore, this research has the potential to make a significant contribution, particularly in terms of a more in-depth comparison of the two financing models and how they can support the sustainability and development of SMEs in Indonesia.

RESEARCH METHODOLOGY

This study uses a qualitative approach with a literature study method. The data used is sourced from scientific journal articles, OJK and banking publications, news, and online articles from credible sources. Literature searches were conducted through Google Scholar, Sinta, and Connectedpaper to obtain relevant and high-quality articles. Literature searches were also conducted through news and articles from credible mass media. The literature search was conducted using keywords such as 'Fintech and MSMEs,' 'Banking Financing,' 'Financial Access,' and others in journal databases and academic search engines. Journal and official report selection was conducted by considering the publication year within the range of 2019-2025. The approach in collecting and selecting these sources aims to obtain accurate and reliable data (Utami, NBR., et al. 2024). The collected data was then analysed using content analysis, which involves reading and understanding the content of each document or literature source. Then, identifying important information based on specific themes or categories. This comparison is done to identify the strengths and weaknesses of traditional banking and fintech in providing access to financing for MSMEs. This enables MSMEs to make more informed decisions, especially when choosing the right financing. The researchers used the literature review method to produce a comprehensive and in-depth analysis of the effectiveness of traditional banking and fintech services in providing access to financing for SMEs. Additionally, this study is expected to provide policy recommendations to improve access to financing for SMEs in Indonesia.

RESULTS AND DISCUSSION

Traditional Banking Financing for MSMEs

Traditional banking has long been the main source of financing for MSMEs with various credit products such as working capital loans, investment loans, and microcredit. According to previous research, approximately 40% of SMEs do not consider banking as an alternative source of funding for SME development (Rudiyanto, 2022). This is due to differing perceptions among SME entrepreneurs regarding banking, who view bank interest rates as relatively high, thereby burdening their businesses, complex loan application procedures, and onerous collateral requirements. According to Supeni et al (2019), the complex application process, strict credit requirements, and collateral that must be provided make it difficult for many small businesses to meet these criteria. On the other hand, banks view MSMEs as complicated, high-risk, and low-profit. Banks face difficulties in finding potential MSMEs with collateral.

Banks impose strict conditions when disbursing credit to SMEs. Traditional banks are reluctant to provide financing to sectors deemed to have high-risk portfolios, including Micro, Small, and Medium Enterprises (SMEs). Banks that continue to provide financing to high-risk sectors tend to set higher interest rates compared to financing for sectors considered relatively safe. There are several SMEs with certain characteristics that banks tend to avoid when providing financing:

1. Weak financial condition or capital.
2. Low level of business diversification.
3. Low credit rating or even no credit rating at all.
4. High dependence on financing to run the business.
5. Limited access to financing or capital.
6. Insufficient collateral or even no collateral at all.
7. Inadequate collateral or even no collateral at all.
8. Higher transaction costs compared to similar types of businesses.

Price Water House Coopers (2019) conducted a survey which concluded that 74% of Micro, Small and Medium Enterprises (MSMEs) in Indonesia do not have access to finance. This obstacle is mainly due to MSMEs being unable to meet the requirements set by banks. Additionally, limited information and a lack of financial literacy among MSME operators also pose significant barriers to the use of traditional banking services. Based on research from various literature sources, several factors were identified that hinder MSMEs' access to financing from banks (Hasibuan, 2024).

First, MSMEs are not considered eligible for banking services (bankable). Although MSMEs are classified as productive businesses, they still cannot meet the requirements to obtain financing from banking institutions. This is mainly due to the inability of MSMEs to provide collateral or guarantees that meet the requirements set by the bank (Soemitra et al., 2022). Collateral set by banks serves as a safeguard in the event of default or non-payment by the debtor (OJK, 2020). However, on the other hand, if the requirements for applying for financing or credit for MSMEs still require assets as collateral, then most MSMEs will not be able to access financing from banks. Currently, many countries have implemented the concept of credit scoring and no longer apply the collateral or guarantee approach. The SME sector continues to be encouraged to go digital, at least in terms of SME financial record-keeping. This could be a consideration for banking institutions when approving credit applications from SMEs.

Second, there is a lack of understanding among SME operators regarding the mechanisms and requirements for applying for financing. Many SME operators do not understand the mechanisms and requirements set by banks, such as legal documents, business plans, and collateral. This process is often considered time-consuming, even though capital needs are usually urgent. As a result, many SME operators choose a more practical route, namely applying for financing from non-bank financial institutions because the process is

simpler and the disbursement is faster. The lack of understanding of the functions and purposes of the requirements set by banks is a challenge in itself, and it is the responsibility of banks to provide education and socialisation regarding financing procedures (Agustin et al., 2023).

Third, the lack of financial literacy among SMEs. Financial literacy is an important tool that SME operators must possess to more easily manage and develop their businesses (Ardila et al., 2020). The lack of financial literacy is one of the causes of low access to financing from financial institutions (Suryanto & Rasmini, 2018), making it difficult for the SME sector to upgrade to become professional entrepreneurs (Sailendra et al., 2020). Based on the 2022 National Survey of Financial Literacy and Inclusion (SNLIK) by the Financial Services Authority (OJK), the financial literacy index of the Indonesian people was 49.68%, an increase compared to 38.03% in 2019 (Fadhilurrahman, 2023).

Fintech Financing for MSMEs

Fintech refers to a funding model that connects borrowers with lenders through digital platforms to facilitate loans without involving traditional banks (Agosto, 2021). By adopting advanced technology, Fintech Lending offers a more efficient process, wider access, and a much better user experience compared to conventional financing methods (Berg et al., 2021). Fintech has various types of services that are commonly used in SME financing, such as peer-to-peer (P2P) lending, crowdfunding, and other digital lending platforms.

Service speed is one of the key values they offer, enabling business owners to obtain much-needed funds within days, not weeks or months (Suleiman, 2021). This capability is crucial for small business owners who often require immediate funds to seize time-sensitive business opportunities or cover urgent expenses. Fintech lending uses advanced technology to assess creditworthiness, leveraging diverse data including electronic transaction history, social media usage, and peer-to-peer evaluations, to determine a customer's credit eligibility (Serfes et al., 2023). The advantages of this process are not only its speed and convenience but also its ability to provide more personalised and tailored services to meet the needs of small businesses. Through advanced applications and algorithms, fintech lending can make loan decisions quickly and accurately, reduce operational costs typically incurred in the credit approval process, and offer more competitive interest rates (Green, 2021).

However, fintech services also face challenges such as data security risks, the lack of comprehensive regulations, and the need to build public trust, especially among SMEs that are not yet familiar with digital technology. Additionally, there are credit risks such as businesses struggling to repay loans on time, high interest rates, or hidden fees that can strain the cash flow of small businesses, and defaults that can damage a business's reputation. Fintech service providers must ensure data security and user privacy to minimise the risk of data breaches that could erode user trust. The government and financial regulatory agencies must ensure that there is a regulatory framework governing fintech lending operations, including licensing, operational standards, and protective measures for borrowers and lenders. Clear and consistent regulations reduce legal uncertainty and ensure fairness in the market. As a result, consumers feel safer to participate, and service providers can operate effectively within the established legal boundaries. In addition, SMEs can avoid credit risk by conducting in-depth financial analysis of their businesses to ensure that loans can be repaid on time and by researching the platform's reputation, interest rates, and other fees before applying for financing.

Fintech has emerged as a complement, not a competitor, to traditional banking. The two have different market segments and strengths. In the context of financial inclusion, fintech is able to reach groups that have not been touched by formal financial services. However, the sustainability of long-term financing and consumer protection remain the strengths of traditional banking. Therefore, collaboration between banks and fintech is an ideal strategy for creating a more equitable, inclusive, and sustainable SME financing system.

Perbandingan layanan Perbankan Tradisional dan Fintech bagi UMKM

Traditional banking services and fintech differ in several aspects. The differences in question can be seen in the table below:

Table 1. Comparison of traditional banking services and fintech

Aspects	Traditional Banking	Fintech
Application Process	Formal, manual and time-consuming	Digital, fast and easy
Requirements	Collateral, business legality	Minimal documentation, no collateral
Target SMEs	Small to medium scale	Micro-small
Interest rates	Relatively low	Relatively high
Regulations	Strict and structured	Still developing

Traditional banking services are an important part of the financial system that aims to support the growth of the productive sector. Banks provide various facilities such as working capital loans, investment credit, savings, current accounts, as well as payment and transfer services. In addition, some banks also offer business assistance, entrepreneurship training, and access to markets through partnership programmes. Traditional banking services can be the primary choice for MSMEs in accessing financing because they offer relatively stable interest rates, high levels of security and trust, and flexible credit terms. However, traditional banking has drawbacks such as lengthy application processes and the need for collateral and business legalisation. This is useful for protecting banks from risks such as default by debtors.

On the other hand, Fintech serves as an alternative financing option for SMEs not served by traditional banking, particularly those deemed 'bankable' by banks. Fintech offers financing with simpler processes and broader access. Fintech does not require collateral when SMEs apply for financing. It uses advanced technology with algorithms to assess creditworthiness, thereby accelerating the financing decision-making process. On the other hand, Fintech also has several drawbacks, such as relatively high interest rates, data security risks, low user trust, immature regulations, credit risks, and suboptimal customer protection.

CONCLUSION

This study shows that fintech and traditional banking services each have their own advantages and disadvantages in providing access to financing for MSMEs. Fintech excels in speed, inclusiveness, and technological innovation, while conventional banks are stronger in terms of regulation and security. The combination of these two approaches is crucial for expanding access to financing for SMEs nationwide. Moving forward, adaptive regulations and policy support are needed to encourage synergy between fintech and formal financial institutions to drive SME growth.

This study has several limitations, such as a lack of high-quality references, such as Scopus-indexed journals. Therefore, future research is advised to use high-quality reference sources. Additionally, future researchers are advised to use the Systematic Literature Review (SLR) approach to deepen the findings of this study. Researchers may also consider examining the perspective of users regarding traditional banking services or fintech services.

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