

UDC 332

## **BUSINESS INNOVATION: THE DEVELOPMENT OF BUMDES BASED ON SOCIAL AND BUSINESS ORIENTATION**

**Wilopo Wilopo, Susilo Heru\*, Iqbal Mohammad, Fahrudi Agung N.L.I., Alfisyahr Rizal, Sanawiri Brillyanes**

Department of Business Administration, University of Brawijaya, Indonesia

\*E-mail: [heru\\_fia@ub.ac.id](mailto:heru_fia@ub.ac.id)

### **ABSTRACT**

A village-owned enterprise (VOE) is the embodiment of the productive economic management of a village. VOE operates in a cooperative, participatory, emancipatory, transparent, accountable, and sustainable manner. Furthermore, VOE aims to improve the village economy. *Badan Usaha Milik Desa* (BUMDES) is the embodiment of VOE in Indonesia. BUMDES manages rural area development and village community empowerment. Furthermore, BUMDES solves existing problems in the village using a business approach. In addition to being profit-oriented, BUMDES has a social mission. This research aims to describe BUMDES typology based on business and social orientation and determine the existing problem in each typology using the value chain approach. This research uses a qualitative model. The findings reveal that five BUMDES in Malang Regency have a social role and contribute to the community as a social enterprise. In addition, nine BUMDES remained focusing on the economy and profit. The analysis of the BUMDES life cycle shows that BUMDES faced challenges in the initial establishment stage. The problems were related to local leadership, equity capital, and management competence.

### **KEY WORDS**

Village-owned enterprise, mapping the potential, *Badan Usaha Milik Desa*.

A village-owned enterprise (VOE) is the embodiment of the productive economic management of a village. VOE operates in a cooperative, participatory, emancipatory, transparent, accountable, and sustainable manner. Furthermore, VOE aims to improve the village economy (Hidayati, 2015). The most common VOE is Township and Village Enterprises (TVEs)<sup>1</sup>. The rapid growth of TVEs was one of the major successes of the China economic reforms in the 1980s. Furthermore, TVEs played an important role in transitioning from central planning to a market-oriented economy (Huang, 2008; Jefferson, 1998; Kung & Lin, 2007; Naughton, 2007).

TVEs empower local communities as workers. TVEs employed 40 million workers in 1998 through group-owned TVEs. Furthermore, TVEs employed 70 million workers through individually owned TVEs. In addition, TVEs encouraged economic growth in China. Due to the significant economic growth, China has the second-highest economic level in the world.

TVEs have the highest contribution to the Chinese industrial sector, surpassing the public sector, foreign investment sector, and fast-rising private-domestic sector (Chen2000). However, the lack of separation between ownership and control caused management issues (Zhu, 1998). Based on previous research, the factory manager had little room for decision-making and did not obtain shared profit (Cheand Qian, 1998). Walder (1995) stated that the managers had no ownership rights over the company. Regardless of the management issue, China successfully built the state economy by focusing on the rural economy. Therefore, other countries such as Indonesia need to make China a role model.

BUMDES is the embodiment of VOE in Indonesia. BUMDES manages rural area development and village community empowerment. Furthermore, BUMDES solves an existing problem in the village using a business approach. In addition to being profit-oriented, BUMDES has a social mission. However, the village community has not fully accepted

---

<sup>1</sup>TVEs are market-oriented public enterprises under the purview of local governments based in townships and villages in China.

BUMDES implementation. Due to the lack of trust, the BUMDES program could not run optimally. The Indonesian government increases village funds to encourage BUMDES to utilize the funds and foster the community. BUMDES need to employ a social mission and become a social enterprise. Cooney and Shanks (2010) state that social enterprise is an effective method to alleviate poverty. Social enterprise is capable of responding to various poverty dimensions such as social marginalization. The role of BUMDES is one of the bases of this research. It is necessary to map existing BUMDES to determine the social and business orientation. East Java Province is one of the Indonesian provinces with an even distribution of BUMDES. East Java Province has beginner, developing, and developed BUMDES.

Data from kemendes.go.id showed that Malang Regency, East Java Province, Indonesia ranked second of total operating BUMDES with 101 BUMDES. Furthermore, Malang Regency has the highest number of developed BUMDES (42 BUMDES). Therefore, this research was conducted in Malang Regency. This research used a chain value approach to simplify the typology identification process based on business and social orientation. The value chain approach aims to determine problems in each BUMDES typology. Based on the background of the research, this research aimed to describe BUMDES typology based on business and social orientation and determine the existing problem in each typology using the value chain approach.

## LITERATURE REVIEW

### Social Enterprise vs. “Traditional” Enterprise

Cooney and Shanks (2010) state that social enterprise effectively alleviates poverty. Social enterprise is capable of responding to various poverty dimensions such as social marginalization. Social enterprise has attracted practitioners, policymakers, and scholars (MairandMarti, 2006). The practitioners highlight the importance of social entrepreneurs as the element of a community organization to solve local, national, and regional social problems. The social enterprise model allows companies to fulfill social and environmental responsibility. Although traditional profit-making enterprises and social enterprises share many common characteristics, there are unique components that define and characterize the social mission of business organizations. According to Stratan (2017), Rural Support Partners, social enterprise highlights the difference between traditional and social enterprise.

### Value Chain

In general, the BUMDES business unit is similar to a company. Each company design, production, market, distribution, and support their product. The value chain approach is capable of illustrating the BUMDES business unit activity. In other words, the value chain approach describes company strategy and implementation. The value chain approach describes value activities and margin. Value activities are the difference between real company performance (physically) and technology. Margin is the difference between the total value and the collective cost of value activities.

Value activities are divided into two types: main activity and support activity. Main activity refers to production, sales, and after-sales service. Support activity refers to providing materials, human resources, technology, and other functions. Value activities are a unit of several different activities. Value activities form the competitive advantage of a company. How a company combines activity with its economic value will determine cost-efficiency.

### Hybrid Organization

A hybrid organization is an organization model which combines logical elements of organizations (Pache and Santos, 2013). Village level BUMDES and central government level BUMDES used a hybrid organization model as the ownership is shared between the government and private sector. Musacchio & Lazzarini (2014) state that State-Owned Enterprises may obtain more profit compared to other types of organizations. BUMN and BUMDES can adapt and take a different form of organization that differs from a company.

## METHODS OF RESEARCH

This research used a qualitative model. Creswell (2016) states that qualitative research explores and determines social or humanism problems. This research used a qualitative method to explore and determine BUMDES typology based on business and social orientation. Furthermore, this research aimed to explore and determine the existing problem in each typology using the value chain approach. This research employed a case study approach to determine the existing problem in BUMDES.

The data collection used focus group discussion (FGD). FGD produces a descriptive narrative for the research topic (Tracy, 2012; Sholihin et al., 2018). The research object and participants of FGD was BUMDES representative of Malang Regency using the following criteria:

1. BUMDES has been established for at least one year;
2. BUMDES has one or more running or nearly bankrupt business units;
3. The business unit refers to the discussion result of Malang Regency Village Assistant, which was appointed by the Village Government and Ministry of Villages and Development of Disadvantaged Regions. This research involved 14 BUMDES;
4. BUMDES business unit has social and business orientation.

Data analysis in qualitative research aims to interpret data in the form of text, images, or other forms (recordings, videos) obtained from the collection process (Creswell, 2015). The studies are done in different ways, using analytical procedures that are often new and formed while in the field. Despite this uniqueness, the qualitative data analysis process follows certain contours or patterns.

## RESULTS OF STUDY

### Description of BUMDES Joining FGD

This research used the social enterprise theory and the value chain approach to determine the BUMDES typology based on social and business approaches. Furthermore, this research mapped the existing problems using the value chain approach. Therefore, the data collection used a working paper to produce information focused on answering the research problem.

Table1 – BUMDES Establishment Typology

BUMDES Establishment Typology	Description
Spinoff	BUMDES was established from an existing informal business in the village.
Joint Operation Partnership	BUMDES was established to complement existing individual or group-owned businesses in the village.
Asset Revitalization	BUMDES was established from village asset revitalization (previously not managed or undergo function rearrangement).
Village Startup	New BUMDES business initiation based on existing potential and opportunity.

Source: primary data (processed).

Seven BUMDES were established for formality purposes. The BUMDES units were established merely to fulfill the Regulation of the Minister of Village, Development of Disadvantaged Regions Number 4 of 2015 regarding BUMDES establishment. Several BUMDES were established to obtain revolving funds from East Java Province government. The remaining seven BUMDES has various backgrounds for the establishment. BUMDES aims to develop village potential and improve the village economy.

The BUMDES business unit provides a variety of data sources. One to 6 BUMDES units have an active or temporarily suspended operation. Two BUMDES possess one business unit: BUMDES Sejahtera Ngadas (agriculture business unit) and BUMDES Gardam Lestari Ngebruk (waste processing unit). The business sector is dominated by the service sector instead of manufacturing and other sectors. Eight BUMDES runs waste processing units. Five BUMDES runs saving and loan businesses.

The total operation time of the BUMDES business unit is a benchmark to determine the

complexity of the existing problem. Based on data collection, ten BUMDES units have been operating for less than three years. Five BUMDES have been operating for four to eleven years. Based on four typologies of BUMDES establishment, Village Startup BUMDES was established earlier than a spinoff, joint operation partnership, and asset revitalization.

### **Characteristics of BUMDES Joining as FGD Participants Based on Business Life Cycle, Social, and Economy Orientation**

Mapping BUMDES characteristics based on the business life cycle was necessary to determine BUMDES growth rate from a business view. As BUMDES is a social enterprise, determining BUMDES growth rate differs from determining general business growth rate. Churchill and Lewis (1983) developed an organization life cycle that focused on the challenges of small business growth. Churchill and Lewis (1983) state that the organization's life cycle is establishment, survival, success, take-off, and resource maturity. However, small businesses do not necessarily undergo all phases in the aforementioned life cycle. Based on the characteristics of each stage, there were four life cycle stages (Dodge and Robbins, 1992; Kazanjian, 1988; Quinn and Cameron, 1983; Strobl, 2016). The BUMDES life cycle is presented in five stages, referring to BUMDES economy indicators such as profit, break-even point (BEP), or loss. The five stages allow easy identification of BUMDES position in the BUMDES life cycle, which is described as follows:

The first stage of the BUMDES life cycle is the formation stage. BUMDES is recently established and has no activity. The second stage is the validation Stage. BUMDES performs activities through business units. However, these business units have not obtained profit.

The third stage is the growth stage. The established BUMDES business unit has obtained profit (under 1 billion). This stage assumes that BUMDES, with under 1 billion profit, is incapable of providing an adequate salary. The fourth stage is the expansion stage. The established BUMDES business unit has obtained 1 billion to 4.8 billion profit. At this stage, the BUMDES is assumed to have the economic capability to provide an adequate salary. BUMDES in the expansion stage is part of Small and Medium-Sized Enterprise (SME). BUMDES pay taxes similar to SME tax rates. At the expansion stage, BUMDES prepares to become a company.

The fifth stage is the maturity stage. The BUMDES business unit obtained more than 4.8 billion in profit. At this stage, BUMDES is considered a company. Therefore, there are different management systems and activity implementation. Furthermore, the BUMDES tax rate is similar to the company tax rate. BUMDES becomes the village's source of income. The business unit should have assets and capital for expanding the business. BUMDES in the maturity stage is positioned above the previous stages.

The five stages mapped BUMDES position based on an economic level. As BUMDES is a social enterprise, the mapping requires a different approach. According to Stratan (2017), Rural Support Partners and social enterprise highlight the difference between traditional and social enterprise:

1. Objective: social enterprise has a social and/or environmental mission as part of the core objective. Social enterprises seek profit to fulfill social and/or environmental missions.
2. Benefit: in addition to income, the social enterprise produces significant social and environmental benefits for the community.

Furthermore, a social enterprise focuses on social and sustainable innovation. Social enterprise develops a new solution for social issues or uses technology to facilitate problem-solving. Therefore, it is necessary to add a new indicator to map the position of BUMDES based on economic and social orientation.

### **Characteristics of BUMDES' Problems**

#### *Formation Stage*

Village government and BUMDES did not have aspirational local leadership. FGD identification in Malang and Jogjakarta showed problems in local leadership and management.

### *Validation Stage*

#### 1. Identifying Village Potential:

There were inadequate individual abilities and skills in the form of actions, practices, and routines aimed at exploring, integrating, and exploiting business opportunities from the potential of an area. Identifying village potentials refers to the ability to identify opportunities and design business plans based on local potential.

#### 2. Community Participation:

Community participation is local community empowerment to utilize potential by becoming social actors instead of passive subjects, managing resources, making decisions, and controlling livelihood activities. The following are the problems related to community participation:

#### 3. community participation is a recurring problem in the initial establishment of BUMDES:

- there have been different visions between village government (village head) and village aspiration (BUMDES director);
- there has been no common understanding of the crucial role and potency of BUMDES in developing independent villages;
- the village head lacks the vision to develop the village;
- the village head and BUMDES do not understand the role of BUMDES; and
- the village head and BUMDES managers do not understand the role of BUMDES (not including the village capital).

#### 4. Local Entrepreneur Mindset:

The social entrepreneur mindset refers to the interest in utilizing opportunity and solve social problems using limited resources. Social entrepreneurs create value through innovative methods. The social entrepreneur mindset is one of the obstacles in the initial stage of BUMDES establishment. The following are the problem related to the local entrepreneur mindset:

- the individual base ability is crucial for BUMDES management. BUMDES management needs a social entrepreneur mindset to solve village problems;
- there is a lack of creativity in the context of creating products or services;
- there is a lack of social awareness (prosocial and altruism); and
- there is no cohesion between the village community and the sustainability of BUMDES by adhering to community aspiration.

### *Growth Stage*

#### 1. Management and Standardization

This refers to the managerial skill aspect in managing social enterprise organizations and standardizes business operation, products, or services. The following are the problems of management and standardization:

- the technical and conceptual managerial skill in managing financial, production, and human resources, as well as marketing standardized product/services; and
- industry or market eligibility standards.

The following are the quotes of FGD participants (BUMDES, academics, and corporate):

- (Academics and BUMDES) BUMDES managers stated that villages needed assistance and training in human resource development, especially administration, finance, and licensing. The academics expressed a similar statement.

#### 2. Development Strategy:

Development strategy is a crucial aspect to determine the objectives and success of an organization. BUMDES need medium-term strategic planning to grow and develop.

#### 3. Skilled Worker Recruitment

BUMDES need skilled human resources for the organization. The following are problems related to skilled worker recruitment: BUMDES needs to create work opportunities for local human resources; and BUMDES needs to involve and empower local youth to develop the organization.

### *Expansion Stage*

1. Technology:

The village government and BUMDES lacked aspirational local leadership and management. The following is the problems related to technological issues: the need for technology to support BUMDES managerial aspect; and the correct utilization of technology to improve BUMDES production and performance.

2. Business Model and Portfolio Management:

BUMDES managers require advanced managerial skills to manage multiple business units using different business models. The following is the problem related to the business model and portfolio management: the majority of BUMDES has multiple business units. Therefore, the managers require the ability to manage business units using varied business models; and the managers must create innovative business models.

*Maturity Stage*

1. Accountability:

It refers to the ability of BUMDES to provide accountability to all organizational stakeholders for all actions and results. BUMDES is obligated to be accountable for the management and business achievement to the village community, government, and taxation.

2. Adaptability:

It refers to the adaptability level of BUMDES against environmental changes. BUMDES need to strengthen existing competence. Furthermore, BUMDES needs to explore opportunities and new competence (innovation) to improve growth rate, social impact, and sustainability.

## DISCUSSION OF RESULTS

This research used a business and social approach to analyze the influence of BUMDES on the community. Cooney and Shanks (2010) stated that social enterprise effectively alleviates poverty. A social enterprise is capable of responding to various poverty dimensions such as social marginalization. One of the social orientation functions is to reduce poverty and increase economic equity in villages. According to Doherty et al. (2009), social enterprises compete using business skills to achieve social objectives. Similar to other businesses, a social enterprise aimed to sustain the business and obtain profit. Social enterprises utilize entrepreneurial drive to achieve wider social objectives. Social enterprises may reduce the social gap and increase social welfare (Welsh Assembly Government, 2005). Based on the analysis result, there were five socially-oriented BUMDES in Malang Regency. The measurement was based on BUMDES contribution to the village community. Therefore, it is necessary to increase BUMDES effort to influence the community.

Based on the analysis result, there were existing problems on each BUMDES level. The major issues are as follows:

1. Local Leadership:

Social entrepreneurship experiences a series of challenges common to many nascent domains where it is shaped or dominated by only a small number of actors (Nicholls and Cho 2006). The actors or stakeholders in question are selected individuals, foundations and affiliates, and media intermediaries. Stakeholders effectively shape the agenda and initiatives put forward by social entrepreneurs and researchers. Hynes (2009) states that lack of stakeholder and community understanding on social enterprise concept, objective, and benefit will deter social enterprise's growth.

2. Equity Capital:

Equity capital is one of the obstacles to business actors. The ability to seek non-bank funds is crucial for a social enterprise. Equity capital depends on government equity capital and corporate social responsibility (CSR) in the initial phase. Hynes (2009) states that business actors rely on personal funds to start and maintain business operations in the first year. Business actors add funding from commercial financial institutions at later stages.

3. Competence:

The competence of business actors may drive the success or deter the growth of a company such as a social enterprise. Darby and Jenkins (2006) state that social entrepreneurs need to translate their objectives into applicable business strategies. In doing so, the social entrepreneur may measure the sustainability of performance effectively and achieve social enterprise visions. Therefore, it is necessary to form core competence (Imperatori and Ruta, 2006). The competence is measured through the internal factor of social enterprise. Management and standardization, skilled worker recruitment, and technical mastery are common problems in the initial stage of social enterprise establishment.

### CONCLUSION AND SUGGESTIONS

FGD results showed that five BUMDES in Malang Regency have a social role and contribute to the community as a social enterprise. In addition, nine BUMDES remained focusing on the economy and profit.

The analysis of the BUMDES life cycle shows that BUMDES faced challenges in the initial establishment stage. The problems were related to local leadership, equity capital, and management competence.

The Ministry of Village, Development of Disadvantaged Regions needs to empower BUMDES into a business and social enterprise. The empowerment may be conducted through collaboration between universities and business actors.

Further research may focus on the behaviors of BUMDES management and the relationship between BUMDES and village heads (village governments). In doing so, further research may map existing conflicts and minimize BUMDES issues.

### REFERENCES

1. Bruderl, J., & Schussler, R. (1990). Organizational Mortality: The Liabilities of Newness and Adolescence. *Administrative Science Quarterly*, 35(3), 530-547.
2. Che, J., & Qian, Y. (1998). Institutional environment, community government, and corporate governance: understanding China's township-village enterprises. *Journal of Law, Economics, and Organization*, 14, 1-23.
3. Chen, W. (2013). Organisational change and development of reformed Chinese township and village enterprises. *Journal of Org. Change Management*, 26(2), 353 – 369.
4. Churchill, N. C., & Lewis, V. L. (1983). The five stages of small business growth. *Harvard Business Review*, 61(3), 30-50.
5. Cooney, K., & Shanks, T. (2010). New Approaches to Old Problems: Market-Based Strategies for Poverty Alleviation. *Social Service Review*, 84, 29-55.
6. Dodge, H. R., & Robbins, J. E. (1992). An Empirical Investigation of the Organizational Life Cycle Model for Small Business Development and Survival. *Journal of Small Business Management*, 30(1), 27- 37.
7. Hidayati, U. (2015). Performance analysis of village-owned enterprise managers as a basic of designing education and training. *European Journal of Business and Management*, 7(32), 143-147.
8. Huang, Y. (2008). *Capitalism with Chinese characteristics*. NY: Cambridge Univ. Press.
9. Jack, S. L., Dodd, S. D., & Anderson, A. R. (2008). Change and the development of entrepreneurial networks over time: a processual perspective. *Entrepreneurship & Regional Development*, 20(2), 125-159.
10. Jefferson, G. (1998). Are China's rural enterprises outperforming state enterprises? Estimating the pure ownership effect. In G. Jefferson, & I.
11. Kazanjian, R. K. (1988). Relation of Dominant Problems to Stages of Growth in Technology-Based New Ventures. *Academy of Management Journal*, 31(2), 257-279.
12. Kung, J., & Lin, Y. (2007). The decline of township-and-village enterprises in China's economic transition. *World Development*, 35(4), 569-584.