



Governance Frameworks and Resilience of Micro-Enterprises: A Diagnostic Evaluation and the Role of Local Wisdom in Enhancing Sustainability

Gagaring Pagalung¹

Faculty of Economics and Business, Accounting
Department, Hasanuddin University

Marwah²

Faculty of Law, Hasanuddin University

Nuvida RAF³

Faculty of Economics and Business, Accounting department, Hasanuddi
University

Aulia⁴

Faculty of Economics and Business, Muhammadiyah University of Makassar

Abstract

This study aims to examine the governance frameworks of micro-enterprises (MEs) and their ability to survive in a competitive environment. Using the governance diagnostic tool developed by the International Finance Corporation (IFC), which is widely implemented in both developed and developing countries, the study evaluates six key governance areas. It also integrates local wisdom in applying the diagnostic tool. Discussions with micro-enterprise owners in Kendari and Makassar were conducted to assess the implementation of the IFC governance tool, providing insights into the actual governance practices in place. The results show that during the COVID-19 pandemic, micro-enterprises in the food, culinary, and hijab accessory sectors managed to sustain operations. However, from a governance perspective, most micro-enterprises are at the "Basic/Start-Up" stage, with an average score of 0-20% in the IFC matrix, indicating underdeveloped governance structures. Only four of the 15 governance elements were adequately met. These findings highlight significant governance weaknesses and the need for ongoing support to ensure long-term sustainability. The study suggests the introduction of a sustainability index for micro-enterprises, which should be disseminated as a crucial tool for evaluating their long-term viability and guiding policy development for SMEs.

Keywords: Governance, Micro-Enterprises, Sustainability, IFC Matrix.

Introduction

Micro, Small, and Medium Enterprises (MSMEs) are a fundamental pillar of Indonesia's economy, playing an essential role in fostering economic growth, alleviating poverty, and



creating employment opportunities. As reported by the Ministry of Cooperatives and SMEs

(2021), MSMEs contribute approximately 61% to Indonesia's Gross Domestic Product (GDP) and absorb more than 97% of the national workforce. This sector has demonstrated remarkable resilience, particularly during economic downturns, where it has acted as a stabilizing force for the national economy. The strategic importance of MSMEs is further highlighted by their role in supporting economic inclusion, particularly in rural and underserved areas, where they serve as a primary source of livelihood for many communities.

Despite their critical contributions, MSMEs, particularly micro-enterprises, face numerous challenges that hinder their ability to sustain and grow their businesses. Limited access to capital, inadequate infrastructure, and insufficient technological adoption are among the most pressing issues that constrain MSMEs. Moreover, these challenges are exacerbated by Indonesia's diverse geographic and cultural landscape, which often necessitates tailored approaches to business development. The COVID-19 pandemic further highlighted the vulnerabilities of MSMEs, as many were unable to adapt to the rapidly changing economic environment, leading to significant disruptions in their operations. For instance, many micro-enterprises operating in the informal sector lacked the digital infrastructure and financial reserves needed to survive prolonged periods of reduced consumer activity.

Governance has emerged as a critical factor in addressing the challenges faced by MSMEs and enhancing their long-term sustainability. Good governance practices provide a framework for MSMEs to manage resources effectively, reduce operational risks, and respond proactively to dynamic market conditions. Recognizing the importance of governance, the International Finance Corporation (IFC), part of the World Bank Group, developed a governance assessment tool to help MSMEs evaluate and improve their governance structures. This tool has been widely implemented in both developed and developing countries, offering valuable insights into governance maturity and areas requiring improvement. However, the adoption of this governance tool in Indonesia remains limited, particularly among micro-enterprises, which often lack the capacity and resources to implement such frameworks.

The application of governance frameworks in Indonesia also faces unique challenges related to cultural and contextual factors. Indonesia's rich diversity in terms of local customs and practices necessitates the integration of local wisdom into governance models to ensure their relevance and effectiveness. Without this cultural alignment, governance frameworks risk being perceived as overly rigid or inapplicable to the specific needs of MSMEs. This underscores the importance of adapting global governance tools, such as the IFC's framework, to better suit Indonesia's local context, particularly in regions with distinct economic and cultural characteristics.

The focus on MSMEs in Kendari and Makassar is particularly relevant, given their unique economic ecosystems that combine urban and rural characteristics. Data from Badan Pusat Statistik (BPS, 2020) indicate that MSMEs account for over 90% of business activities in these regions and serve as a significant source of employment. However, these enterprises face considerable challenges, including limited access to financial resources, inadequate support from local governments, and weak governance structures. Addressing these issues is crucial not only for the sustainability of individual businesses but also for the broader economic development of these regions.

This study aims to address three main issues. First, it seeks to evaluate the extent to which micro-enterprises in Kendari and Makassar have adopted governance practices based on the IFC diagnostic tool. This includes an assessment of governance maturity and identifying gaps that hinder effective governance. Second, the study aims to identify specific governance elements that are underdeveloped or absent among micro-enterprises in these regions.



Understanding these gaps is essential for developing targeted interventions that can enhance governance practices. Third, the study explores how local wisdom and cultural practices can be integrated into the governance framework to enhance its relevance and applicability for micro-enterprises in Indonesia. The findings of this research are expected to provide valuable insights for policymakers, enabling them to develop more effective and contextually relevant governance policies for MSMEs. By bridging the gap between global governance frameworks and local realities, the study aims to contribute to the advancement of MSME sustainability in Kendari and Makassar. Furthermore, the research underscores the importance of integrating local cultural and economic dynamics into governance frameworks, providing a model that can be replicated in other regions with similar characteristics.

Ultimately, this study seeks to promote inclusive economic growth by enhancing the governance capacity of MSMEs in Kendari and Makassar. By addressing the critical challenges faced by these enterprises, the research aims to support their transition from survival-focused operations to sustainable and growth-oriented businesses. This transition is essential for ensuring that MSMEs can continue to play their pivotal role in driving economic development, reducing poverty, and improving social welfare in Indonesia.

Research Methodology

This study employs a qualitative research design to analyze the extent to which micro, small, and medium enterprises (MSMEs) implement governance practices and to identify governance challenges that hinder their sustainability. The qualitative approach is particularly suitable for this research as it allows for an in-depth exploration of complex phenomena, such as governance practices, within the socio-economic context of micro-enterprises in Kendari and Makassar. This approach provides a comprehensive understanding of how the International Finance Corporation (IFC) governance assessment tool, which consists of six governance areas, is applied and identifies potential areas for improvement. Furthermore, incorporating local wisdom into the governance framework is investigated to ensure its relevance and effectiveness in the Indonesian context.

Research Design

The research design integrates a diagnostic and participatory approach. The diagnostic element focuses on assessing the governance maturity of micro-enterprises using the IFC governance tool. This tool evaluates 15 governance elements, which are categorized under six key areas: board effectiveness, risk management, compliance, accountability, leadership, and strategy (IFC, 2020). Meanwhile, the participatory approach involves engaging micro-enterprise owners in discussions to understand their perspectives on governance implementation, barriers, and the role of local wisdom in strengthening governance frameworks.

This design is aligned with the research objective of evaluating governance practices and identifying gaps that require targeted interventions. By combining diagnostic and participatory methods, the study ensures a comprehensive understanding of governance challenges and opportunities in the unique contexts of Kendari and Makassar. The incorporation of local wisdom is expected to provide practical and culturally relevant solutions for governance improvement.

Research Setting and Participants

The study was conducted in two cities: Kendari and Makassar. These cities were selected due to their diverse economic ecosystems, which represent both urban and rural economic dynamics. The participants of the study included micro-enterprise owners from key sectors such as food processing, culinary services, and fashion accessories (e.g., hijab products), which demonstrated resilience during the COVID-19 pandemic. A total of 30 micro-enterprises, with

an equal distribution between Kendari and Makassar, were purposively sampled based on their willingness to participate and their relevance to the research objectives.

Data Collection Methods

Data collection involved two primary methods:

Diagnostic Governance Assessment: The IFC governance assessment tool was employed to evaluate the governance practices of participating micro-enterprises. Each enterprise was assessed based on the 15 governance elements. The diagnostic scores, which range from 0% to 20% for the basic (start-up) stage, provided quantitative insights into governance maturity levels.

Focus Group Discussions (FGDs): FGDs were conducted with micro-enterprise owners to explore their experiences in implementing governance practices. These discussions focused on understanding the challenges faced in adopting governance frameworks, the elements of local wisdom that could enhance governance, and the support required for sustainability. The participatory nature of FGDs ensured that the voices of micro-enterprise owners were central to the research findings.

Data Analysis

The collected data were analyzed using thematic analysis to identify patterns and themes related to governance practices, gaps, and the integration of local wisdom. The diagnostic scores from the IFC governance tool were triangulated with qualitative insights from the FGDs to provide a holistic understanding of the governance landscape. Thematic analysis followed Braun and Clarke’s (2006) six-phase framework, which includes familiarization with the data, generating initial codes, searching for themes, reviewing themes, defining and naming themes, and producing the report.

Analysis and Result

The findings of this study reveal critical insights into the governance practices of micro, small, and medium enterprises (MSMEs) in Kendari and Makassar. These results provide a comprehensive understanding of the challenges faced by micro-enterprises in implementing governance frameworks, particularly during the COVID-19 pandemic. The main findings are presented in the following sections, accompanied by relevant data summaries and interpretations.

Governance Maturity Assessment

The governance practices of micro-enterprises were evaluated based on 15 key elements, grouped into six major areas: board effectiveness, accountability, leadership, strategy, risk management, and compliance. The results are summarized in Table 1.

Table 1. Governance Maturity Scores of Micro-Enterprises

Governance Element	Average Score (%)	Stage(Category)
Board Effectiveness	12	Basic/Start-Up
Accountability	18	Basic/Start-Up
Leadership	15	Basic/Start-Up
Strategy	10	Basic/Start-Up
Risk Management	8	Basic/Start-Up
Compliance	20	Basic/Start-Up

The findings, as summarized in Table 1, reveal a low overall governance maturity, with an average score of 13.83%, indicating that most enterprises are at the "Basic/Start-Up" stage of governance maturity as defined by the IFC tool.

Among the six governance areas, compliance scored the highest at 20%, reflecting some awareness of regulatory requirements. However, this score remains within the basic category, indicating room for improvement. Conversely, risk management received the lowest score of 8%, highlighting the limited ability of micro-enterprises to anticipate and mitigate risks effectively. Leadership practices scored 15%, while strategic planning scored just 10%, indicating a general lack of focus on long-term goals and decision-making capacity. These findings underscore the need for significant improvements in governance to ensure the sustainability of micro-enterprises.

Sectoral Resilience During COVID-19

The study also examined the resilience of different sectors within the micro-enterprise ecosystem during the COVID-19 pandemic which is shown in Figure 1. It was found that enterprises in the food processing and culinary services sectors, as well as those producing fashion accessories such as hijabs, demonstrated remarkable adaptability and sustained their operations despite the economic downturn.

Approximately 35% of the micro-enterprises in Kendari and Makassar were engaged in food and culinary services, which faced minimal disruptions due to their essential nature. These businesses leveraged local resources and existing demand to maintain operations. Similarly, the fashion accessories sector, which accounted for 25% of micro-enterprises, remained resilient due to the continued demand for hijabs, a culturally significant product. These findings highlight the importance of sector-specific strategies to enhance resilience among micro-enterprises.

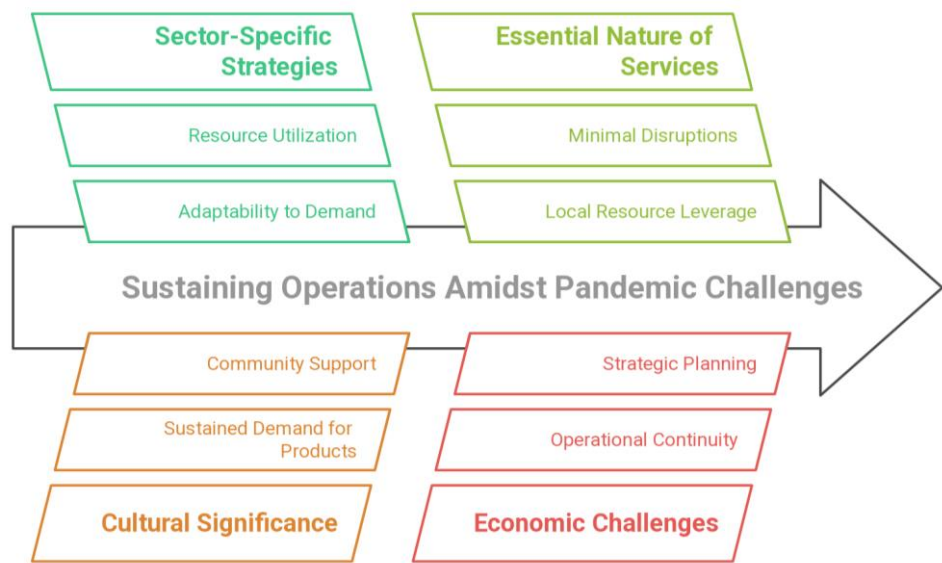


Figure 1. Resilience of Micro-Enterprises During COVID-19

Governance Gaps

Significant governance gaps were identified in the micro-enterprises studied. Only 10% of the enterprises demonstrated a clear understanding of long-term strategic goals, indicating a lack of emphasis on strategic planning. Risk management practices were particularly underdeveloped, with an average score of just 8%, leaving enterprises vulnerable to external



shocks. Leadership practices scored slightly higher at 15%, but still reflected limited decision-making capacity and team management skills. These governance gaps suggest a pressing need for targeted interventions to build the capacity of micro-enterprises in these critical areas.

Integration of Local Wisdom into Governance Frameworks

Focus Group Discussions (FGDs) conducted with micro-enterprise owners revealed the potential for integrating local wisdom into governance practices. Two key elements emerged as valuable contributions to governance frameworks: community-based decision-making and the cultural value of gotong royong (mutual cooperation).

Enterprises that involved community members in decision-making processes reported improved accountability and stronger community support. Additionally, the principle of gotong royong enhanced collective responsibility and resource sharing, fostering a sense of solidarity and resilience. These findings highlight the importance of adapting governance frameworks to incorporate local cultural values and practices, ensuring their relevance and effectiveness in the Indonesian context.

Policy Implications

The findings of this study underscore the need for targeted interventions to enhance governance practices among micro-enterprises. Several policy recommendations are proposed:

Governance Training and Mentorship: Tailored training programs focusing on critical governance areas such as risk management, strategic planning, and leadership should be developed for micro-enterprises. Mentorship programs involving experienced business leaders could further support the capacity-building process.

Localization of Governance Frameworks: The IFC diagnostic tool should be adapted to incorporate local cultural values, such as gotong royong and community-based decision-making, ensuring its applicability and acceptance among micro-enterprises in Indonesia.

Sustainability Index Socialization: A sustainability index tailored to micro-enterprises should be introduced and widely socialized as a benchmark for evaluating and improving governance practices. This index could serve as a valuable tool for both micro-enterprises and policymakers.

Discussion

Governance Maturity and IFC Diagnostic Tool

The findings indicating low governance maturity among micro-enterprises align with earlier studies emphasizing the nascent state of governance structures in small and medium-sized enterprises (SMEs). For instance, Abor and Adjasi (2007) highlighted the significant governance challenges faced by SMEs in developing countries, including limited strategic planning and weak risk management systems. The governance maturity score of 13.83%, as revealed in this study, corroborates these earlier findings, emphasizing that micro-enterprises often prioritize short-term operational concerns over long-term governance structures.

However, this study expands on previous literature by using the IFC diagnostic tool to quantitatively assess governance maturity, a methodological advancement that offers a more nuanced understanding of governance capabilities. The low scores in strategic planning (10%) and risk management (8%) align with the Resource-Based View (RBV) theory (Barney, 1991), which posits that internal capabilities, including governance practices, are critical for achieving competitive advantage. These findings suggest that the micro-enterprises studied lack the internal resources and capacities necessary to anticipate and mitigate risks effectively.



Sectoral Resilience and Adaptability

The resilience observed in food processing, culinary services, and fashion accessories sectors during the pandemic aligns with studies emphasizing sectoral variations in adaptability during economic shocks. For example, Sharma et al. (2020) identified that essential and culturally significant sectors tend to exhibit higher resilience during crises due to sustained demand. The findings of this study also echo insights from the theory of resilience in socio-economic systems (Folke, 2006), which emphasizes the role of local resource utilization and adaptability in maintaining system stability.

The ability of food processing enterprises to sustain operations during the pandemic highlights the importance of leveraging local resources and consumer demand, consistent with the concept of ecological embeddedness (Whiteman & Cooper, 2011). Similarly, the cultural relevance of hijabs in the fashion accessories sector underscores the significance of cultural embeddedness in shaping enterprise resilience, extending the findings of studies such as those by Hampel et al. (2020), which explore the role of cultural practices in business sustainability.

Governance Gaps and Strategic Implications

The study's identification of governance gaps, particularly in strategic planning and risk management, supports earlier research by Beck and Demirguc-Kunt (2006), who highlighted that governance weaknesses leave small enterprises vulnerable to external shocks. The low scores in leadership practices (15%) and strategic planning mirror findings by Ghosh and Roy (2013), who argued that leadership deficits impede decision-making and long-term growth in small enterprises.

However, this study introduces a novel perspective by emphasizing the integration of local wisdom, such as gotong royong (mutual cooperation), into governance frameworks. This approach aligns with the Institutional Theory (Scott, 2008), which underscores the importance of aligning organizational practices with local cultural and institutional contexts. By integrating community-based decision-making and collective resource sharing, this study extends the applicability of governance theories to the unique cultural dynamics of Indonesian micro-enterprises.

Findings and Conclusion

This study aimed to assess the governance practices of micro-enterprises in Kendari and Makassar, identifying key areas for improvement to enhance their sustainability and resilience. The findings reveal that the overall governance maturity of these micro-enterprises is low, with an average score of 13.83%, placing most enterprises at the "Basic/Start-Up" stage according to the IFC diagnostic tool. Among the six governance areas, compliance achieved the highest score (20%), while risk management scored the lowest (8%), highlighting significant weaknesses in risk anticipation and mitigation capabilities.

During the COVID-19 pandemic, micro-enterprises in the culinary and fashion accessory sectors, particularly those producing hijabs, demonstrated notable resilience, leveraging local resources and sustained demand to continue their operations. Furthermore, the study found that integrating local wisdom, such as the practice of gotong royong (mutual cooperation) and community-based decision-making, could strengthen governance frameworks and enhance the relevance of management practices. These findings underscore the importance of adapting governance structures to local cultural contexts to improve long-term sustainability and resilience.

Overall, this study provides valuable insights into the current state of governance in micro-enterprises and highlights the need for targeted interventions to address governance gaps,



particularly in strategic planning and risk management, while incorporating local cultural values. Such efforts will be crucial in fostering the long-term sustainability and resilience of micro-enterprises in Indonesia.

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