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Title: Digitalization and the performances of micro-, small enterprises (MSEs): A case study in Yogyakarta, Indonesia

The world is going digital. Likewise, digital technology is becoming an integral part of life in Indonesia. Little is known how digitalization affect the performance of micro, small enterprises (MSEs), one of the major foundations of the Indonesian economy. MSEs are a source of income and employment for more than 53 million people in Indonesia, yet their productivity is relatively low.

The Indonesian government is boosting its digital economy in which MSEs are among the main players. In the 14th Economic Policy Package, the Indonesian government released an e-commerce road map aiming to be the biggest digital economy in the Southeast Asia with 1,000 “technology entrepreneurs” by 2020. This paper examines the extent of digitalization among MSEs in Indonesia and reveal the impact of internet adoption on labor productivity and export performance.

We conducted MSE survey in Yogyakarta, the most densely MSEs populated province in Java island home to more than 55% of Indonesian people. The identification strategy exploits the fact that the differences in geographic topography produces conceivably exogenous variation in the strength of cellular signal that MSEs in various areas can receive which facilitates them to connect to the internet. We find that digitalization among MSEs is at a nascent stage, with a divide in revenue and demographic features between the internet adopters and non-adopters. The internet utilization is dominated by the use of social media, while those with websites or e-commerce platform is very few. We show that the ICT has enabled MSEs to engage in the digital economy and improved their performance. The internet uptake increases labor productivity and exports.

Hence, this study supports the argument that the digital economy, represented by the access and the use of ICT, has significant potential to contribute to development and inclusiveness by expanding trade opportunities and encouraging financial inclusion. Evidence this study finds is expected to induce a strong justify to develop public policies aiming at fostering firms’ use of the internet. This will not only encourage the government to provide ICT infrastructure but also to increase MSE entrepreneurs’ readiness to benefit from the technology.