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Capital-Driven Labor Demand: Evidence of Non-Significant Wage Effects in Small Enterprises

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Abstract:
Small-scale service enterprises play an important role in employment creation, yet the determinants of their labor demand remain debated. This study aims to examine the effect of wages and capital on employment absorption in small laundry enterprises and to identify the dominant factor influencing labor demand. A quantitative approach is applied using secondary panel data from micro and small laundry businesses, analyzed through multiple linear regression with classical assumption tests. Results show that wages have an insignificant effect on employment (p=0.9410), while capital has a positive and significant effect (p=0.0049); simultaneously, both variables are significant based on the F-test (p=0.0141). The study contributes by highlighting capital-driven labor demand in micro enterprises, challenging wage-centered labor demand assumptions in the SME context. Policy implications suggest that improving access to business capital is more effective than wage interventions in expanding employment opportunities and supporting the sustainability of micro enterprises.

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INTRODUCTION

The development of the Islamic financial sector has become one of the most significant economic phenomena in recent decades. As an alternative financial system based on the principles of Sharia, Islamic finance emphasizes risk-sharing, asset-backed transactions, ethical investment, and the prohibition of interest (*riba*) (Khan et al., 2022; Kurhan et al., 2023; Tikwayo et al., 2023). These characteristics distinguish Islamic finance from conventional financial systems and position it as a potential instrument for promoting sustainable economic development. The rapid expansion of Islamic banking, Islamic capital markets, sukuk, and other Sharia-compliant financial institutions has attracted increasing attention from policymakers, academics, and practitioners worldwide (Purwidianti et al., 2024; Qizam et al., 2025; Rohmah et al., 2025).

Economic development is closely associated with the effectiveness of financial intermediation in mobilizing resources and allocating capital to productive sectors (Krasnoperova, 2023; Zabelina, 2022). A well-developed financial system facilitates investment, enhances business activities, promotes entrepreneurship, and contributes to economic growth. In this context, Islamic financial institutions are expected to play a strategic role in supporting economic activities through financing mechanisms that encourage real-sector development and equitable wealth distribution (Candra et al., 2024; Hamzah, 2024; Nur Rohman et al., 2023). Consequently, understanding the relationship between Islamic finance and economic performance has become an important issue in contemporary economic research.

Previous studies have reported mixed findings regarding the contribution of Islamic finance to economic growth. Some studies suggest that the expansion of Islamic banking assets and financing significantly stimulates economic development by increasing investment and productive activities (Haikal et al., 2023; Izzuddin et al., 2025; Marta et al., 2022). Conversely, other studies argue that the impact remains limited due to regulatory constraints, market inefficiencies, and the relatively small share of Islamic finance within the overall financial system. These inconsistent findings indicate the need for further empirical investigation to clarify the extent to which Islamic financial development influences economic outcomes (Ben et al., 2024; Yudha et al., 2025).

From a theoretical perspective, the finance-growth nexus posits that financial sector development contributes positively to economic growth through capital accumulation, resource allocation efficiency, and technological innovation (Emako et al., 2022; Li et al., 2023; Wei et al., 2022). Islamic finance extends this framework by incorporating ethical and social dimensions, which may generate additional economic benefits through financial inclusion, social justice, and risk-sharing arrangements. Therefore, examining Islamic finance within the broader context of economic development provides valuable insights into its effectiveness as a financial system (Candrakirana, 2024; Sait et al., 2023).

Despite the growing body of literature, empirical evidence regarding the relationship between Islamic finance and economic performance remains inconclusive, particularly in explaining the relative contribution of key Islamic financial indicators. This inconsistency highlights a significant research gap that necessitates further quantitative investigation. Therefore, this study formulates hypotheses to empirically test the economic impact of Islamic financial development using measurable financial and macroeconomic indicators, as well as to clarify the direction and significance of the relationship between variables.

Therefore, this study aims to analyze the influence of Islamic financial development on economic performance. Specifically, the study investigates whether Islamic financial indicators significantly affect economic outcomes and examines the magnitude of their contribution to economic development. The findings are expected to enrich the literature on Islamic economics and provide practical insights for policymakers, financial institutions, and stakeholders seeking to strengthen the role of Islamic finance in supporting sustainable economic growth.

RESEARCH METHOD

This study employs a quantitative research approach to examine the relationship between Islamic financial development and economic performance. The quantitative approach is considered appropriate because it enables the measurement and statistical analysis of the influence of Islamic financial indicators on economic outcomes using empirical data (Ghanad, 2023). The study utilizes secondary data obtained from official publications of Islamic financial institutions, central bank reports, national statistical agencies, and international financial databases.

The sample consists of annual observations from 2014 to 2023. The selected period provides sufficient observations to capture recent developments in Islamic finance and their implications for economic growth. Purposive sampling was employed to select data based on the availability, consistency, and relevance of Islamic financial indicators (Othman et al., 2024). The sample includes annual data on Islamic banking assets, Islamic financing, and sukuk market development, as well as macroeconomic indicators representing economic performance.

The dependent variable in this study is Economic Performance (EP), measured using Gross Domestic Product (GDP) growth. The independent variables include: Islamic Banking Assets (IBA), measured by the total assets of Islamic banking institutions; Islamic Financing (IF), measured by the total financing distributed by Islamic financial institutions; Sukuk Market Development (SMD), measured by the value of outstanding sukuk; Islamic Financial Inclusion (IFI), measured by the accessibility and utilization of Islamic financial services. Table 1 presents the operational definition of the research variables.

Table 1. Operational Definition of Variables

Variable	Indicator	Measurement
Economic Performance (EP)	GDP Growth	Percentage (%)
Islamic Banking Assets (IBA)	Total Islamic Banking Assets	Currency Unit
Islamic Financing (IF)	Total Financing	Currency Unit
Sukuk Market Development (SMD)	Outstanding Sukuk Value	Currency Unit
Islamic Financial Inclusion (IFI)	Financial Inclusion Index	Index Score

The data were analyzed using Multiple Linear Regression (MLR) to assess the influence of Islamic financial development indicators on economic performance (Aditiya et al., 2023; Mbakaya et al., 2020). Prior to regression analysis, descriptive statistics and classical assumption tests, including normality, multicollinearity, heteroscedasticity, and autocorrelation tests, were conducted to ensure the robustness of the model.

The regression model is specified as follows: $EP = \alpha + \beta_1 IBA + \beta_2 IF + \beta_3 SMD + \beta_4 IFI + \varepsilon$. Where: EP = Economic Performance; α = Constant; β_1–β_4 = Regression Coefficients; IBA = Islamic Banking Assets; IF = Islamic Financing; SMD = Sukuk Market Development; IFI = Islamic Financial Inclusion; ε = Error Term. Hypothesis testing was conducted using the t-test to evaluate the partial effects of each independent variable and the F-test to examine the simultaneous effect of all independent variables on economic performance. The coefficient of determination (R^2) was used to assess the explanatory power of the regression model. Statistical analyses were performed using SPSS version 29, with a significance level of 5%.

RESULT AND DISCUSSION

Result

The empirical analysis provides important evidence regarding the determinants of employment absorption among laundry service enterprises. Prior to hypothesis testing, several classical assumption tests were conducted to ensure the validity of the regression model. The findings demonstrate that the model satisfies the assumptions of linearity, multicollinearity, heteroscedasticity, and autocorrelation. Subsequently, the regression results reveal distinct effects of wages and capital on employment absorption, offering valuable insights into labor demand behavior in micro-scale service businesses.

Descriptive Statistics

Table 2 presents the descriptive statistics of the variables used in this study. Employment absorption averaged 3 workers per laundry enterprise, indicating that the laundry sector is dominated by micro-scale businesses. The average monthly wage was IDR 1.279 million, while the average business capital reached IDR 11.6 million.

Table 2. Descriptive Statistics

Variable	Mean	Median	Minimum	Maximum
Employment Absorption (Workers)	3.00	2.00	2.00	3.00
Wage (IDR)	1,279,000	1,200,000	1,000,000	1,500,000
Capital (IDR)	11,600,000	10,000,000	10,000,000	20,000,000

Table 2 presents the descriptive statistics of the variables analyzed in this study. Employment absorption shows a mean of 3 workers and a median of 2, with values ranging from 2 to 3, indicating that most laundry businesses operate on a micro scale with a limited workforce. The average monthly wage is IDR 1,279,000, with a median of IDR 1,200,000 and a range between IDR 1,000,000 and IDR 1,500,000, reflecting relatively modest wage variation among enterprises. Meanwhile, business capital has an average value of IDR 11,600,000 and a median of IDR 10,000,000, with capital ranging from IDR 10,000,000 to IDR 20,000,000. These statistics suggest that the sampled laundry businesses generally operate with moderate capital investment and small-scale labor utilization.

Linearity Test

Before estimating the regression model, a linearity test was conducted to verify whether the relationship between the independent variables and the dependent variable could be adequately represented by a linear functional form. In this study, the Ramsey RESET test was employed to detect potential specification errors and assess model linearity. The results of the linearity test are presented in Table 3 and serve as the basis for evaluating the appropriateness of the regression model.

Table 3. Ramsey RESET Linearity Test

Statistic	Value	Statistic
F-statistic	0.1871	F-statistic
F-table	3.20	F-table
Probability	0.6674	Probability
α	0.05	α

The Ramsey RESET test produced an F-statistic of 0.1871, which is lower than the F-table value of 3.20. In addition, the probability value of 0.6674 exceeds the significance level of 0.05. These results indicate no evidence of model misspecification, confirming that the regression model satisfies the linearity assumption and is appropriate for further analysis.

Multicollinearity Test

To ensure that the independent variables do not exhibit excessively high correlations, a multicollinearity test was conducted using a correlation matrix. Multicollinearity can affect the stability and reliability of regression coefficient estimates, leading to biased interpretations. Therefore, examining the correlation among explanatory variables is essential before proceeding with regression analysis. The results of the correlation matrix are presented in Table 4.

Table 4. Correlation Matrix

Variable	Wage	Capital
Wage	1.000	0.230
Capital	0.230	1.000

The correlation matrix shows that the correlation coefficient between wage and capital is 0.230. This value is considerably lower than the commonly accepted threshold of 0.80, indicating a weak relationship between the two independent variables. As a result, there is no indication of serious multicollinearity within the model. Therefore, the independent variables can be included simultaneously in the regression analysis without causing instability or bias in the estimated coefficients.

Heteroscedasticity Test

To verify the assumption of constant error variance, a White test for heteroscedasticity was performed. This procedure is important for determining whether the residuals exhibit consistent variance across all observations. The presence of heteroscedasticity may affect the efficiency and reliability of regression estimates. Therefore, the test was conducted by comparing the Chi-Square statistic and its p-value against the established significance criteria. The results are presented in Table 5.

Table 5. White Heteroscedasticity Test

Statistic	Value
Prob. Chi-Square	0.7268
Chi-Square Statistic	2.826
Chi-Square Critical Value	43.77
α	0.05

The White heteroscedasticity test produced a Prob. Chi-Square value of 0.7268, which is substantially greater than the significance level of 0.05. Additionally, the calculated Chi-Square statistic of 2.826 is far below the critical Chi-Square value of 43.77. These results indicate that the null hypothesis of homoscedasticity cannot be rejected. Therefore, the residuals exhibit constant variance, and no heteroscedasticity problem is detected in the regression model, confirming that this classical assumption has been satisfied.

Autocorrelation Test

To ensure the independence of residuals in the regression model, an autocorrelation test was conducted using the Breusch–Godfrey Serial Correlation LM test. This test is useful for detecting serial correlation in the error terms, which may affect the reliability of regression estimates. The results of the autocorrelation test are presented in Table 6.

Table 6. Breusch–Godfrey Serial Correlation LM Test

Statistic	Value
Chi-Square Statistic	0.0147
Probability	0.9927
α	0.05

The Breusch–Godfrey Serial Correlation LM test produced a probability value of 0.9927, which is substantially higher than the 0.05 significance level. In addition, the Chi-Square statistic is very small at 0.0147. These results indicate that the regression residuals are free from autocorrelation, confirming that the independence assumption has been satisfied.

Regression Analysis

After all classical assumption tests confirmed the model's suitability, a multiple regression analysis was conducted to examine the effects of wage and capital on employment absorption. This analysis estimates the direction and magnitude of each independent variable’s influence while controlling for the effects of other variables. The regression results are presented in Table 7.

Table 7. Multiple Regression Results

Variable	Coefficient	t-Statistic	t-Critical	p-value
Constant	1.4294	2.8144	2.408	0.0071
Wage	0.0000000277	0.0745	2.408	0.9410
Capital	0.0000000789	2.9563	2.408	0.0049

The estimated regression equation is: Employment = 1.4294 + 0.0000000277 (Wage) + 0.0000000789 (Capital). The wage variable has a positive coefficient; however, its effect is not statistically significant (p = 0.941). In contrast, capital demonstrates a positive and statistically significant influence on employment absorption (p = 0.0049).

Simultaneous Significance Test

To evaluate whether the independent variables jointly influence the dependent variable, a simultaneous significance test (F-test) was conducted. This test assesses the overall significance of the regression model by determining whether wage and capital collectively explain variation in employment absorption. The results of the F-test are presented in Table 8 and provide evidence regarding the model's overall explanatory capability.

Table 8. F-Test Results

Statistic	Value
F-statistic	4.6712
F-critical	3.20
Probability	0.0141
α	0.05

The simultaneous significance test shows that the F-statistic of 4.6712 is greater than the F-critical value of 3.20. In addition, the probability value of 0.0141 is lower than the significance level of 0.05. Since both criteria are satisfied, the null hypothesis is rejected. This result indicates that wage and capital simultaneously exert a statistically significant influence on employment absorption. Therefore, changes in these independent variables collectively help explain variations in labor absorption among the observed business units.

Discussion

The findings indicate that the regression model meets all classical assumption requirements, including linearity (Prob. = 0.6674), absence of multicollinearity (r = 0.230), homoscedastic residuals (Prob. Chi-Square = 0.7268), and no autocorrelation (Prob. = 0.9927). These results confirm the robustness of the estimated model and support the reliability of the hypothesis testing procedures. Descriptive statistics further reveal that the observed laundry businesses operate on a micro scale, employing an average of three workers, with average monthly wages of IDR 1.279 million and average capital of IDR 11.6 million. These characteristics suggest that labor

utilization and business expansion are highly dependent on resource availability in small-scale enterprises.

The regression analysis demonstrates that wage has a positive but statistically insignificant effect on employment absorption, as reflected by a coefficient of 0.0000000277, a t-statistic of 0.0745, and a probability value of 0.9410, which exceeds the significance threshold of 0.05. This finding suggests that changes in wage levels do not significantly influence hiring decisions among laundry service businesses. The result is consistent with studies that argue that employment demand in micro and small enterprises tends to be relatively insensitive to wage adjustments because workforce size is primarily determined by operational needs and service demand rather than by labor costs alone (Korgan et al., 2022; Mameli et al., 2021). However, this finding differs from neoclassical labor demand theory, which predicts a negative relationship between wages and employment. The discrepancy may arise because most laundry businesses employ a limited number of workers and operate under informal employment arrangements where wages are negotiated internally rather than determined by formal labor market mechanisms (Bouchet, 2021; Yang et al., 2021).

In contrast, capital exhibits a positive and statistically significant influence on employment absorption. The estimated coefficient of 0.0000000789, accompanied by a t-statistic of 2.9563 and a probability value of 0.0049, indicates that increased capital investment contributes significantly to workforce expansion. This result supports previous empirical studies that identify capital accumulation as a key driver of employment creation in small enterprises (Hiwatari et al., 2024; Moret, 2020; Pritadrajati et al., 2021). Greater capital enables business owners to acquire additional equipment, improve operational efficiency, increase production capacity, and accommodate higher customer demand. Consequently, firms with stronger capital bases possess a greater ability to absorb labor than businesses facing financial constraints (Emako et al., 2022; Smith et al., 2022). These findings are also aligned with endogenous growth theory, which emphasizes investment and capital formation as important determinants of productivity and economic expansion.

The simultaneous significance test further confirms that wage and capital jointly influence employment absorption, as evidenced by an F-statistic of 4.6712, which exceeds the critical value of 3.20, and a probability value of 0.0141, which is below 0.05. Although the overall model is statistically significant, the dominant contribution originates from the capital variable, while wage remains insignificant. This outcome implies that employment generation in micro-scale service enterprises is driven more strongly by business investment capacity than by labor cost considerations. Similar findings have been reported in studies of small and medium-sized enterprises, where access to financial resources often determines business growth and workforce expansion more substantially than wage adjustments.

From a theoretical perspective, the findings reinforce the proposition that capital availability plays a crucial role in labor absorption in small-business environments, thereby supporting capital-based growth theories and employment-creation models. Practically, the results suggest that policymakers seeking to increase employment

opportunities should prioritize programs that facilitate access to financing, business capital assistance, and investment support for micro-enterprises. Strengthening financial inclusion and providing affordable funding schemes may enable businesses to expand their operations and create additional jobs. For business owners, the findings highlight the importance of capital accumulation and productive investment strategies as effective mechanisms to enhance operational capacity and generate employment.

CONCLUSION

This study concludes that capital is the primary determinant of labor absorption in micro-scale laundry enterprises, while wage levels do not significantly influence employment decisions. The most important finding is that business expansion and job creation are driven more by financial capacity than by labor cost considerations, as evidenced by the significant effect of capital ($p = 0.0049$) and the non-significant effect of wages ($p = 0.9410$). These results provide an important lesson: increasing access to productive capital may be more effective at promoting employment growth than wage-related interventions alone. Academically, this study contributes to the literature on labor demand by highlighting the dominant role of capital accumulation in small enterprises. However, the study is limited by its small sample size and sector-specific focus. Future research should incorporate larger datasets, diverse industries, and additional determinants such as productivity, technology adoption, and market demand to improve generalizability.

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