

Analysis of the Role of Financial Literacy and Financial Inclusion on the Financial Performance of MSMEs

Ika Wisudawaty¹

¹Makassar State University, Indonesia

Nur Arisah²

²Makassar State University, Indonesia

Corresponding Author: ika.wisudawaty@unm.ac.id

Abstract

This study aims to comprehensively analyze the role of financial literacy and financial inclusion on the financial performance of MSMEs in Indonesia through a literature review from various reputable national and international sources. The results show that good financial literacy encourages MSMEs to make more informed financial decisions, improve the quality of financial reports, and strengthen risk management capabilities. Meanwhile, financial inclusion expands MSMEs' access to capital, insurance, and digital payment services, thereby increasing business efficiency and competitiveness. However, challenges remain, particularly in the 3T (frontier and remote) regions, such as disparities in access, limited infrastructure, and a dominant cash transaction culture. Therefore, integrated policy interventions are needed in the form of contextual financial literacy education, strengthening the digital financial ecosystem, and improving infrastructure. This study is expected to serve as a reference for researchers, practitioners, and policymakers in formulating sustainable MSME empowerment strategies in the digital era.

Keywords: Financial Literacy, Financial Inclusion, Financial Performance, MSMEs, Literature Review

INTRODUCTION

Many developing countries rely on micro, small, and medium enterprises (MSMEs) as a pillar of the country's economy and developed countries. At the global level, MSMEs account for more than 90% of the number of businesses and around 60-70% of employment, thus playing a significant role in promoting inclusive economic growth and poverty alleviation (World Bank,

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IJEVSS, Volume 04 Issue 04, 2025



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2023). In Indonesia, the role of MSMEs is even more dominant. With a significant contribution, MSMEs account for more than 60% of the national Gross Domestic Product (GDP) and absorb around 97% of the workforce in Indonesia, according to data collected by the Ministry of Cooperatives and SMEs, MSMEs are the main foundation in maintaining the stability and sustainability of the national economy.

In the midst of this strategic role, MSMEs face various challenges that can hinder the potential for business growth and sustainability. One of the main challenges is the weak financial management carried out by MSME actors. Many business actors still rely on manual financial recording, even most of them do not record at all. This condition causes difficulties in monitoring cash flow, determining the cost of production, and managing debts and receivables effectively (Tabrani et al., 2025).

The low level of financial literacy is a major cause of weak financial management in MSMEs. Financial literacy is the ability of individuals to recognize financial concepts, risks, and products, as well as have skills in managing finances wisely. Lusardi, (2014) emphasized that low financial literacy has an impact on improper financial decision-making, both in personal life and in running a business. This also has implications for low investment levels, inaccuracies in working capital management, and inability to anticipate business risks.

In addition, limited access to formal financial services is also a significant problem. Many MSMEs still rely on informal sources of financing, such as loans from families or loan sharks, due to the difficulty of meeting the administrative and collateral requirements set by formal financial institutions. According to Utami et al., (2025) low financial inclusion causes MSME actors to be unable to take advantage of various financial products and services that support business growth, such as people's business credit, insurance, and digital payment services.

The problem of financial literacy and inclusion is increasingly complex in the current era of digitalization. Digital transformation in the financial sector offers a great opportunity for MSMEs to improve operational efficiency and expand the market through digital financial technology (*fintech*). However, many small and medium enterprises (MSMEs) do not have the necessary knowledge and skills to utilize this technology, leaving them behind in an increasingly competitive market competition.

The lack of training and mentoring related to financial literacy and the use of digital financial services is the main obstacle in increasing the capacity of MSME actors (Fitriani et al., 2024). Existing financial education programs often do not reach all MSME actors, especially in remote areas. In addition, there are still obstacles in terms of uneven technology infrastructure



and internet networks throughout Indonesia, thus widening the gap in financial access.

The impact of low financial literacy and inclusion on the financial performance of MSMEs is very real. Many MSMEs experience difficulties in managing cash flow, allocating working capital, and facing financial risks that can threaten business continuity. The inability to access formal financing also limits opportunities for product expansion and innovation, making it difficult for MSMEs to grow and compete in the wider market (Marsenta et al., 2024).

Various studies state that increasing financial literacy and financial inclusion can have a positive impact on the financial performance of MSMEs. Business actors who have a good financial understanding tend to be able to manage business finances more effectively, make more rational investment decisions, and utilize formal financial services to support business development. Financial inclusion also opens access to various financial products that help MSMEs manage risk and expand business networks.

The government and various related institutions have made efforts to improve financial literacy and inclusion among MSMEs through financial education programs, providing easier access to financing, and developing a digital financial ecosystem. However, these efforts still experience various challenges, including a lack of resources, low interest of MSME actors in participating in training, and cultural and social barriers that affect people's financial behavior (Riyani & Virgi, 2025).

Until now, a comprehensive study that simultaneously analyzes the role of financial literacy and financial inclusion on the financial performance of MSMEs in Indonesia, especially in the context of the digitalization era, is still limited. Most studies are still partial, focusing only on one aspect, without looking at the simultaneous and synergistic relationship between the two (Putri et al., 2024).

Therefore, this study aims to comprehensively analyze the role of financial literacy and financial inclusion on the financial performance of MSMEs in Indonesia. Through a literature review from various reputable journal articles, it is hoped that the results of this study are also expected to enrich the literature and become a reference for researchers, practitioners, and policymakers who are interested in strengthening MSMEs in Indonesia.

METHOD

This research applies a qualitative approach that aims to obtain a deep understanding of the phenomena experienced by the research subject holistically, in accordance with the definition put forward by , namely research that seeks to understand the meaning, process, and dynamics



that occur in the natural context through descriptions in the form of words and language. This approach was chosen because it is able to provide a comprehensive and in-depth picture of the issues being researched, especially related to financial literacy, financial inclusion, and financial performance of MSMEs in the Indonesian context (Waruwu, 2024).

The method used in this study is *library research*, which is by examining and analyzing the results of previous research both from the national and international scopes that have been published in reputable journals in the last ten years. Literature review is one of the effective methods to identify, evaluate, and synthesize various relevant scientific findings, so that it can provide a strong theoretical and empirical foundation for this research Suprpto (2022)

The secondary data collection process is carried out through searching for scientific articles on several leading databases such as Google Scholar, ResearchGate, Scopus, and Sinta. The use of these databases aims to ensure a wide and relevant coverage of the literature, as well as to obtain credible and up-to-date data sources. In the search process, the researcher used specific keywords, including "financial literacy", "financial inclusion", "financial performance of MSMEs", and "financial performance of MSMEs", to obtain search results that were in accordance with the focus of the research.

All articles obtained are then selected based on relevance to the research topic and the quality of publications, with priority given to articles that contain empirical research results, theoretical studies, and conclusions that can support the analysis in this study. Literature selection is carried out systematically to ensure that only sources that meet the criteria are used in the further analysis process.

Furthermore, the collected data was analyzed by a qualitative descriptive method, where the researcher identified, categorized, and interpreted the main findings from various literature sources. This analysis aims to uncover patterns, relationships, and trends that have developed in previous studies related to financial literacy, financial inclusion, and financial performance of MSMEs.

This method also provides flexibility in integrating various theories and empirical findings, so that it can provide a complete and in-depth picture of the issue being studied. In its implementation, this research follows systematic stages, starting from determining the topic and focus of the research, searching the literature, selecting sources, analyzing content, to preparing synthesis and conclusions. Each stage is carried out in a careful and structured manner so that the results of research can be scientifically accounted for and make a real contribution to the development of science and practice in the field. Overall, the qualitative approach through



literature review provides a solid foundation to understand the complexity of the problems faced by MSMEs, as well as offer relevant solutions based on the results of scientific studies that have been tested. Thus, this research is not only descriptive, but also analytical and reflective of the dynamics that occur in the field (Asrifan, 2021) .

RESULTS AND DISCUSSION

Based on literature reviews from various national and international studies, it was found that the financial performance of MSMEs in Indonesia is significantly influenced by financial literacy and financial inclusion. The study (Kusumawati et al., 2023) found that MSME actors who have good financial knowledge tend to make wiser and more appropriate financial decisions, such as in budget preparation, cash flow management, and effective business risk mitigation. This ability has a direct impact on improving the financial performance of MSMEs as measured from profitability, liquidity, and solvency of the business.

Financial literacy helps MSMEs to understand and use financial information when making decisions. Research at the Palu City Business Incubator (2023-2024) in (Saharuddin et al., 2025) shows that most small and medium enterprises (MSMEs) understand the basic principles of financial management, such as credit management, savings, investment, and risk management. However, the overall level of financial literacy is still in the medium category, so the application of this knowledge in daily business practices is not optimal. Therefore, in order for financial literacy to be used effectively in business management training, intensification and practical assistance are very important.

In addition, research (Ulfah, 2024) emphasizes that financial inclusion measured through ease of access, use, and quality of formal financial services significantly increases the chances for MSMEs to obtain financing, insurance, and other financial services needed in business development. Financial inclusion also allows MSMEs to reduce their dependence on informal sources of financing which often have high risk and inefficient costs.

Research by (Munzirwan, 2024) strengthens these findings with the conclusion that MSMEs that have better access to formal financial services are able to improve operational efficiency, expand markets, and strengthen the competitiveness of their businesses. Good financial performance of MSMEs, which is characterized by healthy profitability, liquidity, and solvency, is easier to achieve by business actors who manage their finances professionally and make optimal use of formal financial products.

Research (Yazid, 2025) shows that although the level of financial literacy of small and



medium enterprises (MSMEs) is moderate, most MSME actors already have a good understanding of the basic principles of financial management, using money wisely, saving regularly, and disclosing and mitigating financial risks. However, there are still gaps in the consistent application of literacy in daily business management, so intensive training and assistance are needed so that financial literacy can be implemented optimally.

The OJK National Financial Literacy Survey (2019) in (Suleiman et al., 2022a) reported that the level of financial literacy in Indonesia is still relatively low, especially among MSME actors, with only around 38% of MSME actors having a good understanding of financial literacy. This causes many difficulties for MSMEs in preparing accurate financial statements and making the right financial decisions, thereby reducing trust from external parties such as investors and financial institutions.

Financial literacy is the main foundation in MSME financial management. Knowledge and skills in managing finances not only help business actors in preparing a thorough financial plan, but also improve their ability to identify risks and make rational investment decisions. (Junia et al., 2025) states that financial literacy contributes to wiser financial behavior and supports sustainable business growth.

Financial literacy is not only related to the ability to understand financial products and services, but also includes skills in managing business finances as a whole. MSME actors who have financial literacy tend to be able to carry out careful financial planning, manage cash flow effectively, and anticipate financial risks that may arise. This is very important considering that MSMEs often face liquidity challenges and limited capital that can hinder their business continuity (Fitriani et al., 2024a). Thus, financial literacy is the main foundation for MSMEs to increase their power and optimize the resources owned by businesses in the long term.

Understanding basic concepts such as cash flow management, budget planning, credit management, savings, investment, and risk management is the key to the success of MSMEs in managing business finances. The study (Arrezqi et al., 2024) revealed that financial literacy has a significant positive influence on the performance of culinary MSMEs, with financial management as an intervening variable that strengthens this relationship. With increased financial literacy, MSME actors can manage their finances better so that business performance increases significantly.

Good financial literacy also plays a role in improving the quality of MSME financial statements. Accurate and relevant financial statements are essential to assist MSMEs in accessing funding sources and making informed business decisions. (Ayu Rahmawati, 2025) found a strong



correlation (coefficient of 0.65) between the level of financial literacy and the quality of MSME financial statements in Indonesia. Therefore, improving financial literacy must be a top priority in the MSME empowerment program.

Financial inclusion has a positive impact through easy access to formal financial products and services. With wider access, MSMEs can obtain the business capital needed for product expansion and development, utilize insurance as a business risk protection, and use digital payment services that increase business efficiency. (Wahyuni et al., 2025) emphasized that financial inclusion reduces MSMEs' dependence on informal financing sources which tend to be high-risk and expensive.

Financial inclusion plays an important role in strengthening MSMEs' access to a wide range of formal financial products and services that are essential for business development. With easy access to financing, insurance, and digital payment services, MSMEs can increase capital capacity and manage business risks more effectively. (Richard et al., 2024) emphasized that financial inclusion is able to reduce MSMEs' dependence on informal financing sources that often have high interest rates and large risks, thereby improving business stability and sustainability. In addition, financial inclusion encourages MSMEs to transform towards more professional and structured financial management, which ultimately increases the competitiveness of businesses in an increasingly competitive market.

OJK data (2022) in (Suleiman et al., 2022a) shows that the level of financial inclusion in Indonesia is much higher than the level of financial literacy which is still below 50%. This indicates that even though access to financial services is quite wide, the understanding and ability of MSMEs to use these services optimally still needs to be improved. Therefore, financial inclusion programs must be carried out with financial literacy education so that MSMEs can utilize financial services effectively and sustainably.

Although financial literacy and inclusion have received attention from the government and financial institutions, there are still a number of challenges that hinder the improvement of MSMEs' financial performance. One of the main challenges is the low level of financial literacy in remote areas and 3T (Frontier, Outermost, Disadvantaged) areas. Research (Ningsih et al., 2023) revealed that only about MSMEs in the region have access to formal financial services, much lower than in urban areas.

In addition, cultural factors and cash transaction habits are still very dominant among traditional MSMEs, so many business actors are reluctant to take advantage of digital and formal financial services. The lack of equitable education and suboptimal digital infrastructure are also



significant obstacles in increasing the financial literacy and inclusion of MSMEs.

One of the main challenges is the geographical disparity that leads to inequality of access and financial literacy. Research (Yazid, 2025) revealed that MSMEs in the 3T (Frontier, Outermost, Disadvantaged) areas that have access to formal financial services are much lower than 74% in urban areas. Limited infrastructure and education are the main factors that hinder financial inclusion and literacy in the region.

In addition, cultural factors and cash transaction habits are still very dominant among traditional MSMEs. As many as 63% of traditional business actors are reluctant to use digital financial services due to their preference for cash transactions and lack of trust in new technologies. This is exacerbated by the lack of comprehensive digital literacy education and uneven infrastructure, thus hindering the implementation of formal and digital financial services (Khoiriyah & Amalia, 2023).

To address these challenges, integrated policy interventions are urgently needed (Iriani et al., 2024). Some of the strategies recommended based on the literature review are:

1. Contextual and sustainable financial literacy training and education, using real-life case study-based modules that are relevant to the conditions of MSMEs in various regions, including remote areas.
2. Strengthening the digital financial ecosystem through collaboration between governments, financial institutions, fintech, and academia to Develop inclusive products that are easily accessible and understandable by MSMEs.
3. Improving technology infrastructure and internet access in 3T areas so that MSMEs can make optimal use of digital financial services.
4. Providing incentives and ease of regulation for MSMEs that adopt formal and digital financial services, thereby encouraging Accelerating Financial Inclusion

Increasing knowledge and inclusion about finance not only has an impact on the financial performance of MSMEs on a micro level, but also strengthens the competitiveness and longing of the MSME sector as the backbone of the national economy (Iko Putri Yanti, 2019). With better financial management and access to adequate financing, MSMEs have the ability to increase production, increase markets, and create new jobs (Ar Rafi et al., 2024). This is in line with the government's goal to reduce poverty and economic growth through the empowerment of MSMEs.



CONCLUSION

Financial literacy and financial inclusion have been proven to have a significant and positive influence on the financial performance of MSMEs in Indonesia. Financial literacy strengthens the ability of MSME actors to manage their finances professionally and make informed decisions, while inclusive finance opens up access to capital and formal financial services that are essential for business development. The main challenges faced are low financial literacy and limited access in remote areas as well as cultural factors that still hinder the use of digital financial services. Therefore, integrated policy interventions are needed in the form of sustainable financial literacy education, strengthening the digital financial ecosystem, and improving infrastructure so that MSMEs can maximize their potential and make an optimal contribution to the national economy.

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