

## Unlocking MSME Performance: The Role of Financial Literacy Through Financial Management and Competitive Advantage

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**Abstract:** *This research examines how financial literacy can improve MSME performance, with financial management and competitive advantage as mediating variables. Using a quantitative survey of 140 MSMEs in Sidoarjo and SEM-PLS software for analysis, these findings show important and new insights into economic issues. First, MSME performance is not directly impacted by financial literacy. Instead, its impact is fully mediated by competitive advantage and financial management. Second, financial literacy significantly improves financial management practices and strengthens competitive advantage, both of which positively and significantly affect MSME performance. These results demonstrate that financial knowledge alone is insufficient to improve performance unless translated into structured financial practices and strategic differentiation. In real-world conditions, MSMEs that implement systematic bookkeeping, cash flow control, cost efficiency strategies, and product differentiation are more likely to achieve higher profitability and sustainable growth. The study contributes theoretically by extending the Resource-Based View, positioning financial literacy as an internal capability that enhances performance indirectly through managerial and strategic mechanisms. Practically, the findings provide an evidence-based framework for policymakers and MSME practitioners to design targeted financial literacy programs integrated with hands-on financial management training and competitive strategy development.*

**Keywords:** *Competitive advantage; Financial management; Financial literacy; MSMEs performance*

**Abstrak:** *Penelitian ini mengkaji bagaimana peran literasi keuangan dapat meningkatkan kinerja UMKM dengan pengelolaan keuangan dan keunggulan kompetitif sebagai variabel mediasi. Penelitian dilakukan terhadap 140 UMKM di Sidoarjo dengan metode kuantitatif dan penggunaan analisis data SEM-PLS. Temuan penelitian menghasilkan temuan utama dan kebaruan terkait isu-isu ekonomi. Pertama, kinerja UMKM tidak secara langsung dipengaruhi oleh literasi keuangan. Namun, sepenuhnya dimediasi oleh keunggulan kompetitif dan manajemen keuangan. Kedua, literasi keuangan mampu berpengaruh positif pada variabel pengelolaan keuangan serta keunggulan kompetitif. Ketiga, adanya pengaruh positif antara keunggulan kompetitif dan pengelolaan keuangan terhadap kinerja UMKM serta berperan sebagai mediator penuh dalam hubungan antara literasi keuangan UMKM dan kinerja UMKM. Temuan ini menegaskan bahwa pengetahuan keuangan tidak serta-merta meningkatkan kinerja apabila tidak diimplementasikan dalam praktik manajerial dan strategi bisnis yang konkret. Dalam konteks nyata, UMKM yang menerapkan pencatatan keuangan secara sistematis, pengendalian arus kas, efisiensi biaya, serta strategi diferensiasi produk menunjukkan kinerja yang lebih stabil dan berkelanjutan. Secara teoretis, penelitian ini memperluas perspektif Resource-Based View dengan menempatkan literasi keuangan sebagai*

*kapabilitas internal yang berdampak tidak langsung terhadap kinerja melalui mekanisme manajerial dan strategis. Secara praktis, hasil penelitian ini memberikan dasar empiris bagi perumusan program peningkatan literasi keuangan yang terintegrasi dengan pelatihan pengelolaan keuangan dan penguatan keunggulan kompetitif UMKM.*

**Kata kunci:** *Keunggulan kompetitif; Kinerja UMKM; Literasi keuangan; Pengelolaan Keuangan*

**Citation:**

Maghfiroh, R. U., Agustin, R. (2026). Unlocking MSME Performance: The Role of Financial Literacy Through Financial Management and Competitive Advantage. *Iqtishoduna*, 22(1), 20-43. <https://doi.org//10.18860/iq.v22i1.37120>

**INTRODUCTION**

In this era, Micro, Small, and Medium Enterprises (MSMEs) are a sector that supports economic improvement and public welfare in Indonesia. MSMEs contribute to the availability of informal employment, community welfare, and increased community income. As many as 45.2 million national workers have been employed by MSMEs, according to data from the Ministry of MSMEs (Biro DTI, 2025) This contribution means that all parties must provide support so that MSMEs can continue to grow and become more competitive, thereby becoming a resilient sector in the economy. One example of government support is through programs such as guidance, training, and funding. The existence of MSMEs is not only important for national economic growth but also has profound social significance, as it opens up employment opportunities for groups of people who are not accommodated in the formal sector. In many cases, MSMEs are the only alternative for the lower-middle class to earn an income. Therefore, the sustainability of MSMEs directly improves the community's quality of life. In the context of inclusive development, MSMEs are an instrument that links economic growth with social welfare (Susanti *et al.*, 2023)

Despite the fact that a large amount of the literature examining financial literacy and MSME performance, existing and developing studies predominantly emphasize direct relationships between financial literacy and business outcomes. Empirical findings remain inconclusive, with some studies reporting a positive direct effect and others reporting insignificant relationships. These inconsistencies indicate that the mechanism through which financial literacy translates into performance remains theoretically underexplored. In particular, limited attention has been paid to explaining the indirect pathways linking financial literacy to firm performance via internal managerial and strategic capabilities. Therefore, this study advances the literature by proposing and empirically testing a mediated model in which financial literacy enhances MSME performance indirectly through financial management and competitive advantage. This integrative mechanism represents the primary novelty of this research.

The role of MSMEs is evident across various regions in Indonesia, for example, in Sidoarjo Regency, which is one of the centers of small and medium industries in East Java, with more than 250,000 MSME business units (Sidoarjo Cooperative and MSME Office, 2023). The dominant business sectors include food and beverages, fashion, handicrafts, and services. However, despite their large numbers, there are still shortcomings in business management and development, resulting in suboptimal MSME performance. Efforts are required to help MSMEs remain sustainable by

improving their human resources' knowledge of financial management. Good financial management is essential for business operators, making knowledge of financial literacy, financial management, and competitive advantages important factors in improving MSME performance.

Sidoarjo Regency provides a theoretically relevant research setting due to its high concentration of MSMEs across manufacturing, culinary, and creative sectors, combined with strong industrial linkages to Surabaya and East Java's supply chains. The region represents a competitive MSME ecosystem characterized by rapid business growth alongside persistent financial literacy challenges. This dual condition makes Sidoarjo an appropriate context for examining how internal capabilities determine performance outcomes in a dynamic, semi-industrialized environment.

The use of financial management and competitive advantage as mediating variables is theoretically grounded in the capability transformation logic of the Resource-Based View (RBV). Financial literacy alone does not automatically generate superior performance; rather, it must be translated into effective financial management practices such as budgeting, cash flow control, and investment planning (Hererra *et al.*, 2023). These practices enhance operational efficiency and reduce financial risk. Subsequently, efficient financial management enables firms to allocate resources strategically, fostering product differentiation, cost leadership, and market responsiveness, thereby creating competitive advantage. Therefore, financial management and competitive advantage function as sequential mechanisms for building capabilities that transmit the effects of financial literacy to MSME performance. This mediation logic clarifies why financial literacy may not exhibit a direct effect on performance in certain contexts.

Financial literacy challenges are one of the fundamental obstacles faced by MSMEs. A survey by the Financial Services Authority (OJK, 2022) shows that Indonesians' financial literacy index is only 49.68%, while their financial inclusion index is 85.10%. This shows that access to financial services is widespread, but the ability to understand and manage finances is still low. This condition affects the weak recording of transactions, cash flow management, and business planning carried out by MSMEs. Many business actors mix personal finances with business finances, making it difficult to know the real condition of the business (Santoso *et al.*, 2023). Another study by (Meldona *et al.*, 2023) states that knowledge management and financial literacy influence the performance of MSMEs in Malang Raya area; this evidence indicates that MSMEs are likely to achieve higher levels of performance dependent on their ability to effectively acquire and implement knowledge, as evidenced by their expertise in knowledge management and financial literacy.

Financial literacy encompasses an individual's financial decisions, which require sufficient knowledge and confidence to make the right choices that affect their short-term and long-term financial well-being. Enhancing the financial literacy of proprietors and executives is a significant mechanism for mitigating informational asymmetries and collateral inadequacies, especially in loan applications, which are a fundamental component of MSMEs' financial well-being. Scholarly literature is acknowledged as a critical source of competitive leverage. In their study, Hussain (2018) argues that a comprehensive understanding of financial statements, budgets, and financial ratios helps mitigate information asymmetry, thereby enhancing competitive advantage and economic efficiency. Numerous scholars have likewise

demonstrated that financial literacy has a significant impact on competitive advantage (Ernestivita, 2023; Sugangga *et al.*, 2023; Worokinasih *et al.*, 2023) The ability to navigate financial management, investment strategies, and risk assessment effectively is paramount for MSMEs to overcome fiscal adversities and sustain their competitive edge in a dynamic market landscape, which may be a critical determinant of enduring success and resilience in the marketplace. In addition, research findings (Hasan *et al.*, 2024) the research has effectively demonstrated that financial literacy, entrepreneurial acumen, and digital economic proficiency exert a positive and substantial impact on the success of MSMEs.

The rapid development of digital technology today presents both opportunities and challenges for MSMEs. On the other hand, the emergence of digital accounting applications, e-commerce platforms, and fintech services can help MSMEs record their finances, expand their market reach, and improve transaction efficiency. However, MSME actors with low financial literacy are at risk of misusing these technologies, for example, having difficulty reading digital financial reports or making unwise online funding decisions. Jamilah & Mardiana (2024) emphasize that the synergy between financial literacy and digital technology adoption has been proven to increase the competitiveness of MSMEs, especially in facing increasingly fierce competition in the digital economy era.

In an increasingly competitive market, competitive advantages based on differentiation are necessary for SME operations, especially in developing markets, to maintain high performance (Yang *et al.*, 2018). For MSMEs, differentiation does not always have to be expensive or complex, but can be achieved through the authenticity of local products, the use of quality raw materials, or creative marketing strategies that are in line with consumer trends. By implementing the right differentiation, MSMEs are not only able to attract new consumers, but also retain customer loyalty, increase competitiveness, and strengthen their position in the global supply chain (Sugangga *et al.*, 2023)

The higher an individual's level of financial literacy, the greater their financial management skills. Financial literacy influences how people think about their financial situation and also influences decision-making and financial management in their business (Kodu *et al.*, 2023). Several studies also confirm that financial literacy encourages entrepreneurs to take new opportunities. For example, MSMEs that understand finance are more courageous in entering the digital market and exporting because they are able to calculate the potential profits and risks. This becomes a competitive advantage amid global competition (Ernestivita, 2023)

Financial literacy is also closely related to the capability to manage risk because business actors will be better prepared to face market fluctuations, changes in raw material prices, and the risk of default. With good financial literacy, MSMEs can develop risk mitigation strategies, such as preparing reserve funds, diversifying products, and implementing more flexible marketing strategies (Nurjannah *et al.*, 2023). Financial literacy not only serves as a technical skill in managing finances, but also as strategic capital that enables MSME actors to be more disciplined in preparing emergency funds and more careful in assessing potential business risks.

Low financial literacy often leads MSME actors to rely solely on intuition in running their businesses. For example, product pricing is determined without clear production cost calculations, or investment decisions are made without considering the risks. As a result, many MSMEs face cash flow difficulties and eventually go

bankrupt. Conversely, business actors with strong financial literacy can prepare simple reports, understand cash flow, and develop long-term financial plans. This shows that financial literacy is not only a technical skill, but also key to strategic decision-making (Worokinasih *et al.*, 2023). Poor financial management negatively impacts business performance, so it plays an important role in improving MSME performance.

On the other hand, low financial literacy among MSMEs not only hinders financial record keeping but also impacts access to capital. Many financial institutions require simple financial reports to assess loan eligibility, while most MSME actors are not yet able to compile them. As a result, they are more dependent on informal sources of financing with high interest rates, which in turn has the potential to suppress business performance. Research by Dahrani *et al.* (Dahrani *et al.*, 2022) confirms that an increase in the financial literacy of business actors is directly proportional to an increase in opportunities for access to healthier and more sustainable formal financing.

Financial literacy has a direct impact on competitive advantage and financial performance (Hererra *et al.*, 2023). The study shows that competitive advantage can mediate the relationship between financial literacy and the financial performance of MSMEs, such that the higher the financial literacy of business actors, the greater the opportunity for MSMEs to create competitive advantages that improve financial performance. However, different results were shown by another study which stated that financial literacy does not directly affect the performance and competitive advantage of MSMEs in Banyumas (Hanifah & Innayah, 2024). These differing findings indicate the existence of contextual factors, such as regional differences, business owner characteristics, industry type, and level of access to resources and technology, which can influence the relationship between financial literacy and MSME performance.

This study focuses on MSMEs, which assume a critical function in propelling progress in Indonesia and augmenting job opportunities, economic empowerment, and social welfare for individuals who do not have access to formal employment. MSMEs also face fundamental challenges, namely limited financial literacy, limited financial management, and the need to improve competitive advantages in order to enhance MSME performance. Given these challenges, this study will examine the role of financial literacy in improving financial management, competitive advantages, and MSME performance. This study will contribute to several things. To begin with, this inquiry will yield important theoretical contributions pertaining to the effects of financial literacy, financial management, and competitive advantage on the success of MSMEs. Thus, this study is poised to generate meaningful practical outcomes and an extensive framework that can be proficiently applied by MSMEs in developing regions, with a specific focus on Indonesia, to enhance and boost MSME performance.

This study adopts the Resource-Based View (RBV) as the primary theoretical foundation to explain the relationships among the variables. According to RBV, firm performance is determined by valuable, rare, inimitable, and non-substitutable (VRIN) internal resources and capabilities. Within this framework, financial literacy is conceptualized as an intangible cognitive capability that enables entrepreneurs to process financial information and make rational economic decisions. However, RBV suggests that capabilities must be embedded in organizational routines to generate sustained competitive advantage. Accordingly, financial management represents an

operational capability derived from financial literacy, while competitive advantage reflects the strategic outcome of effectively mobilized internal resources. By positioning financial literacy as a foundational capability that operates through managerial and strategic mechanisms, this study strengthens the theoretical coherence of the proposed model.

## **LITERATURE REVIEW**

### **Resource Based View (RBV)**

The Resource-Based View (RBV) serves as the primary theoretical foundation of this study. RBV posits that firm performance is determined by internal resources and capabilities that are valuable, rare, inimitable, and non-substitutable (Barney, 1991). Within this perspective, competitive advantage arises not merely from market positioning but from the effective mobilization of internal intangible capabilities. In the case of MSMEs, financial literacy can be conceptualized as a cognitive intangible resource, financial management as an operational capability derived from that resource, and competitive advantage as the strategic outcome of effectively deployed capabilities. By framing these variables within RBV, this study explains MSME performance as the result of capability transformation rather than isolated financial knowledge.

The concept of RBV was developed in 1950 as a business development strategy model used to analyze and estimate resources in the form of tangible and intangible assets owned by an organization so that they can be used to achieve sustainable competitive finance (Aisyah *et al.*, 2022). In the context of MSMEs, the application of RBV theory is very relevant because most MSMEs have limitations in access to capital and distribution networks. Therefore, they must optimize the resources they have, such as labor skills, local product quality, and good relationships with customers. Recent research by Timotius (2023) confirms that the competitive advantage of MSMEs is often born from the use of unique resources that competitors do not have, such as typical food recipes, crafts based on local wisdom, or emotional closeness to consumers.

### **MSME Performance**

Performance is the results achieved by an organization during a certain accounting period based on predetermined goals and criteria (Kase *et al.*, 2024). Performance in an organization or company can be seen from the level of sales, the rate of return on capital, and the number of market shares that the company has successfully controlled. Measuring the performance of MSMEs is not an easy thing because many MSME entrepreneurs only focus on their operational activities and ignore financial reporting and accounting records. In the research of Sagian, et al. 2019, stated that the performance of MSMEs can be influenced by factors such as: first, Sales growth, second, Capital growth, third, Labor growth, fourth, Market growth, and Profit growth.

### **Financial Literacy**

Financial literacy encompasses the comprehension of financial principles, competencies and proficiencies associated with financial concepts, expertise in business management, and the capacity to execute strategic, relatively accurate, and timely business decisions under specific circumstances (Buchdadi *et al.*, 2020).

Furthermore, the Financial Services Authority (OJK) in 2016 the concept of financial literacy encompasses more than merely comprehending the offerings and functionalities provided by financial institutions. This comprehensive financial literacy enables individuals to establish financial objectives, formulate strategic financial plans, manage their fiscal resources effectively, and engage in prudent financial decision-making regarding the utilization of financial products and services. The domain of financial literacy is categorized into four distinct indicators, which include comprehension of personal finance, mastery of credit management, knowledge of savings and investment, and proficiency in risk management. Although financial literacy and financial management are closely related, they represent conceptually distinct constructs. Financial literacy refers to the cognitive understanding of financial concepts, including budgeting, credit management, investment, and risk assessment. It reflects knowledge and analytical capacity. In contrast, financial management refers to the behavioral and organizational implementation of that knowledge through structured financial practices such as bookkeeping, cash flow control, capital allocation, and financial planning. Within the RBV framework, financial literacy constitutes a foundational resource, whereas financial management represents an applied capability (Kasenda & Wijayangka, 2019). This distinction clarifies that knowledge alone does not guarantee effective financial decision-making unless translated into consistent managerial routines.

### **Financial Management**

Financial Management is an activity that involves the acquisition, funding, and management of assets with several overarching goals (Kodu *et al.*, 2023) Financial management is a series of processes, both planning, implementation, reporting, and financial supervision, which can be carried out by individuals, organizations, companies, and governments to be able to achieve the expected goals. Financial management indicators are divided into 4 aspects, namely planning, recording, reporting and control.

### **Competitive Advantage**

According to the resource-based view (RBV), firms that possess competitive advantages are better able to withstand business challenges and sustain their performance (Hanifah & Innayah, 2024). Competitive advantage delineates a corporation's capacity to exceed rivals by providing enhanced value to clientele, either via reduced pricing or through elevated advantages that substantiate increased expenditures. In practice, competitive advantage can be developed through strategies that leverage internal resources and capabilities, such as creating unique products, maintaining consistent quality, and offering attractive prices to attract and retain customers. For instance, product differentiation based on local wisdom has been identified as a distinctive advantage that is difficult for competitors to imitate (Gunawan *et al.*, 2023). Moreover, service quality and brand image also contribute to enhancing customer value. In the digital era, competitive advantage is increasingly associated with the ability of SMEs to adapt to technological developments and market dynamics, including the adoption of digital marketing, e-commerce platforms, and technology-based innovations to expand market reach and improve operational efficiency (Ernestivita, 2023). This shows that competitive advantage is not only determined by price or product quality alone, but also by the ability to innovate and

the accuracy of strategies in responding to changes in the dynamic business environment. Competitive advantage indicators are divided into three aspects: product uniqueness, product quality, and competitive price.

### **Financial literacy on the performance of MSMEs**

In the context of MSMEs, financial literacy encompasses the ability of business actors to keep financial records, manage cash flow, understand access to capital, and develop short-term and long-term financial plans. A good level of financial literacy will help MSME actors manage capital efficiently, minimise risk, and take advantage of existing business opportunities. The performance of MSMEs is measured by various indicators such as increased sales, profit growth, market share expansion, and the ability to maintain business sustainability. MSME actors with adequate financial literacy will be better able to develop appropriate business strategies, control operational costs, and improve resource efficiency. This not only has implications for improving financial record-keeping, but also impacts the quality of managerial decision-making oriented towards business growth. Therefore, financial literacy serves as an important factor that can drive overall MSME performance improvement. A number of previous studies also reinforce the positive relationship between financial literacy and business performance. Raharjo *et al.* (2023) shows that financial literacy contributes to the sustainability of small businesses through good financial management. Other studies in Indonesia (Nurjannah *et al.*, 2023) also confirm that adequate financial literacy can improve the effectiveness of financial recording and management, which ultimately has an impact on the growth of MSMEs.

Prior studies have produced mixed findings regarding the direct relationship between financial literacy and MSME performance. From an RBV perspective, this inconsistency can be explained by the transformation logic of capabilities. Financial literacy does not automatically generate performance outcomes because cognitive resources must first be embedded into organizational processes. Without structured financial management practices, financial knowledge remains latent and underutilized. Therefore, financial literacy influences performance indirectly by enhancing managerial efficiency and strategic positioning.

H1 : Financial literacy influences the performance of MSMEs

### **Financial literacy on MSME financial management**

Financial literacy plays an important role in shaping good financial management behaviour in MSMEs. Business actors who understand basic financial concepts will be better able to prepare simple financial reports, record transactions neatly, and allocate funds according to business needs. This is the main foundation for maintaining the financial stability of MSMEs. Financial literacy skills also help MSME entrepreneurs in budgeting, managing cash flow, and preparing emergency funds. With these skills, entrepreneurs can minimise errors in financial decision-making, such as avoiding wasteful spending or inappropriate use of capital. Ultimately, good financial literacy will be reflected in sound financial management practices. Previous research supports the notion that financial literacy has a positive effect on SME financial management (Astuti & Soleha, 2023). This means that the higher the level of SME operators' understanding of financial concepts, the better their financial management practices will be. Therefore, financial literacy is an important factor in improving the quality of SME financial management.

H2 : Financial literacy influences the financial management of MSMEs

### **Financial literacy to the competitive advantage of MSMEs**

The competitive advantage of MSMEs can be built through the ability to manage available resources effectively, including financial resources. Financial literacy provides MSME actors with the knowledge and skills to manage capital, manage debt, and develop appropriate investment strategies. Thus, financial literacy can improve business competitiveness in the market. In addition, financial literacy enables MSMEs to be more adaptable to changes in the business environment. Business actors who have a good understanding of finance will find it easier to identify opportunities, reduce costs, and allocate funds for product or service innovation. This can strengthen the position of MSMEs in competition, thereby creating a sustainable competitive advantage. Previous research shows that financial literacy contributes to MSMEs in improving their competitiveness (Sugangga *et al.*, 2023). With good financial management, MSMEs can focus more on improving product quality, operational efficiency, and marketing strategies. Therefore, financial literacy is one of the key factors that can support the creation of competitive advantages in MSMEs.

H3 : Financial literacy influences the competitive advantage of MSMEs

### **Financial management of MSME performance**

Financial management is an important aspect of MSME sustainability. With good financial management, business owners can maintain financial stability, control cash flow, and ensure that available funds are used appropriately. This will have an impact on achieving better business performance, both in terms of profitability and growth. MSME owners who are disciplined in keeping financial records and budgeting will be better able to identify potential financial problems early on. In addition, good financial management can assist in business expansion planning, debt fulfilment, and operational cost control. All of these contribute directly to improving the financial performance of MSMEs. Previous research confirms that there is a positive relationship between financial management and SME performance (Mali, 2023). The better the financial management, the higher the business performance. Therefore, financial management is an important variable that SMEs need to pay attention to in order to achieve business success.

H4 : Financial management influences the performance of MSMEs

### **Competitive advantage to the performance of MSMEs**

Competitive advantage is the ability of MSMEs to create added value and differentiate themselves from competitors. MSMEs with competitive advantages are usually able to offer products with better quality, more competitive prices, or superior service. This factor contributes to increased customer satisfaction and ultimately improves business performance. In addition, the competitive advantage possessed by MSMEs can be a strategy for facing market challenges. With high competitiveness, MSMEs can survive in conditions of intense competition and economic fluctuations. This makes business performance more stable and sustainable. Previous studies have shown a significant relationship between competitive advantage and business performance (Hariandi, 2019). MSMEs that focus on creating competitive advantages will find it easier to increase revenue, profitability, and business growth. Therefore, competitive advantage is a strategic

factor in improving MSME performance.

H5 : Competitive advantage influences the performance of MSMEs

### **The role of financial management in mediating the influence of financial literacy on the performance of MSMEs**

The mediating role of financial management is theoretically justified by capability development theory within RBV. Financial literacy enhances the entrepreneur's ability to interpret financial information, but only through systematic financial management practices can firms improve cost control, liquidity stability, and investment efficiency. These operational improvements directly influence financial performance. Consequently, financial management functions as the mechanism that transforms cognitive capability into measurable business outcomes.

Financial literacy indirectly affects the performance of MSMEs through financial management. MSME actors with high levels of financial literacy will be better able to manage their business finances effectively, which ultimately supports the achievement of optimal business performance. Thus, financial management can act as a mediator in the relationship between financial literacy and SME performance. Good financial management allows financial literacy to be applied in real business activities, such as recording transactions, managing cash flow, and planning investments. Without effective financial management, financial literacy will only be knowledge that is not implemented, so that its impact on business performance will be limited. Previous research supports that financial management plays an important role as a mediating variable ( Dewi & Mahyuni, 2025). This means that financial literacy will be more effective in improving MSME performance if it is supported by good financial management. Therefore, financial management can be considered a mechanism that bridges the correlation between financial literacy and MSME performance

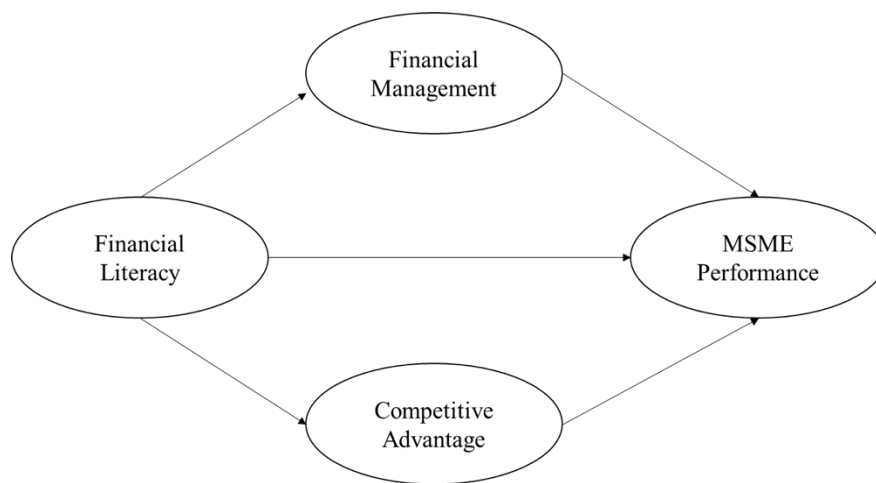
H6 : Financial management acts as a mediating variable in the relationship between financial literacy and SME performance.

### **The role of competitive advantage in mediating the influence of financial literacy on the performance of MSMEs**

Financial literacy is one of the important factors that influence the ability of MSME actors to manage their businesses and achieve optimal performance. However, financial literacy does not always have a direct impact on business performance, but can have an indirect effect through competitive advantage. MSME actors with high financial literacy tend to be better able to manage resources, make financial strategies, and make the right decisions. This ability can then be translated into competitive advantages, such as cost efficiency, product innovation, and better service, which ultimately improve MSME performance. The role of competitive advantage as a mediator is important because financial literacy will only provide tangible benefits when applied in business strategies that are capable of creating competitiveness. For example, financial knowledge enables SMEs to reduce production costs, set competitive prices, or allocate funds for innovation activities. This provides added value that distinguishes SMEs from their competitors, thereby increasing consumer appeal and strengthening their position in the market. Thus, competitive advantage can be considered as the pathway linking financial literacy to improved SME performance.

H7 : Competitive advantage acts as a mediating variable in the relationship between financial literacy and SME performance.

Previous studies have also shown that financial literacy has a significant relationship with competitive advantage, and competitive advantage in turn affects business performance. This confirms that competitive advantage can mediate the relationship between financial literacy and MSME performance (Hererra et al., 2023). This shows that higher levels of financial literacy among business actors enhance their capacity to develop competitive advantages, which in turn contribute to improved business performance. Accordingly, this study posits that competitive advantage functions as a mediating variable that reinforces the impact of financial literacy on MSME performance.



**Figure 1. The Conceptual Model**

As shown in Figure 1, it can be explained that this research has one independent variable (financial literacy) and one dependent variable (MSME performance) as well as two intervening variables (financial management and competitive advantage) or variables that influence the independent and dependent variables. this investigation was carried out to ascertain the impact of the two independent variables on the dependent variable, as well as the factors that affect both the independent and dependent variables.

## RESEARCH METHOD

This study uses a quantitative survey research method on MSMEs in Sidoarjo, which aims to analyze and provide an overview of the correlation of financial literacy, competitive advantage, and financial management on MSME performance. The researcher limited the research location to Sidoarjo. This research was carried out by surveying MSMEs across several business sectors in several sub-districts of Sidoarjo. The research was conducted in July-August 2025. The population in this study consisted of MSMEs in Sidoarjo. The sampling technique used was cluster sampling (area sampling) taken in 18 sub-districts in Sidoarjo. A sample of 140 MSMEs (MSME actors that have been operating for more than 5 years) was obtained by multiplying the number of indicators by 10. This research used quantitative data from primary

sources, distributing questionnaires that respondents answered, and was reinforced by observations of the respondents. This study also used secondary data on the number of MSMEs in Sidoarjo and on previous research on financial literacy and MSME performance.

The variables in this study include the dependent variable (Y), which is the performance of MSMEs in Sidoarjo; the independent variable (X), which is financial literacy; and the intervening variables (Z1), which is competitive advantage, and (Z2), which is financial management. Data measurement in this research uses a Likert scale. The analysis techniques in this study are descriptive analysis and Structural Equation Modelling (SEM) analysis with the help of SmartPLS version 4.0 software. Hypothesis testing was conducted to determine whether the hypotheses formulated theoretically were consistent with the results provided by the SEM-PLS application program. After the structural model met the requirements, the next step was to test the regression weight/loading factor. This test was conducted in the same way as the t-test for regression weight/loading factor/model coefficient. Ferdinand (2014) explained that the t-value was calculated by looking at the CR value and the p-value. A hypothesis is said to have an effect when the CR value produced is  $\geq 1.96$ . Then, for the p-value, it is said to have an effect when the p-value produced is  $\leq 0.05$  (Ghozali, 2017).

This research utilized a quantitative explanatory framework through the implementation of a survey methodology to find out the interconnections between financial literacy, competitive advantage, financial management and the performance of MSMEs in the Sidoarjo Regency, East Java. Sidoarjo was selected due to its strategic economic position, high concentration of MSMEs across 18 sub-districts, and diverse sectoral composition, making it a relevant context for analyzing internal capability-performance linkages. The population consisted of MSMEs registered in the region, and cluster (area) sampling was applied at the sub-district level, with proportional selection within each cluster using official MSME directories. A total of 140 MSME actors who had operated and executed their businesses for more than 5 years were selected to ensure managerial experience and performance stability. Sample adequacy was justified using the 10-times rule and SEM-PLS recommendations for models with moderate complexity. Data were gathered utilizing systematically designed questionnaires employing a five-point Likert scale, supported by limited non-participant observations for contextual validation. Measurement instruments were adapted from established prior studies to ensure content validity. Data were analysed using PLS-SEM with SmartPLS 4 software, using a two-stage procedure, (1) evaluation of the measurement model (convergent validity, discriminant validity, and reliability) and (2) assessment of the structural model using bootstrapping (5,000 subsamples), with hypotheses considered significant at t-values  $> 1.96$  and p-values  $< 0.05$ .

## **RESULT AND DISCUSSION**

### **Result**

MSMEs in Sidoarjo are growing rapidly due to their strategic location near Surabaya, Juanda Airport, and large industrial areas, facilitating distribution and market access, thereby contributing to employment in Sidoarjo. There are several dominant types of businesses, namely in the food and beverage (culinary) sector, such as shrimp crackers, smoked milkfish, petis, and processed seafood specialties

from Sidoarjo. The creative and handicraft industry sector: batik, bags, shoes, sandals, and handicraft trinkets. And the trade and services sector: grocery stores, fashion, and digital-based services that are starting to grow.

According to the Sidoarjo Regency Cooperative and Micro Business Office, as of 2021, there were 13,075 MSMEs spread across 18 sub-districts with different types of businesses, each facing their own challenges, namely the low level of financial literacy among business actors, resulting in suboptimal financial recording and management. Access to capital remains an obstacle for some MSMEs that are not yet bankable, and digital technology adoption is not yet widespread, especially among micro-scale MSMEs. In addition, there is potential for MSME development in Sidoarjo, including its brand image as a region that produces processed marine products and creative industries, which can be further developed. Its strategic location and proximity to a major city (Surabaya) provide opportunities for market expansion. With improved financial literacy, better business management, and strengthened competitive advantages, Sidoarjo MSMEs have the potential for more sustainable growth.

The performance of MSMEs in Sidoarjo was the focus of this study, which collected data from questionnaires distributed to 140 respondents who were food and beverage MSME entrepreneurs spread across 18 subdistricts in Sidoarjo and engaged in various business sectors. Of the respondents in this study, 59.3% or 83 were female and 40.7% or 57 were male. The majority of respondents in this study, or 39.3% or 55 people, were aged 26-35 years, while 36.4% or 51 people were aged 35 years and above, and 24.3% or 34 people were aged 15-25 years. The majority of respondents in this study, 72.1% or 101 people, were high school graduates, while the rest were elementary school, junior high school, diploma and bachelor's degree graduates.

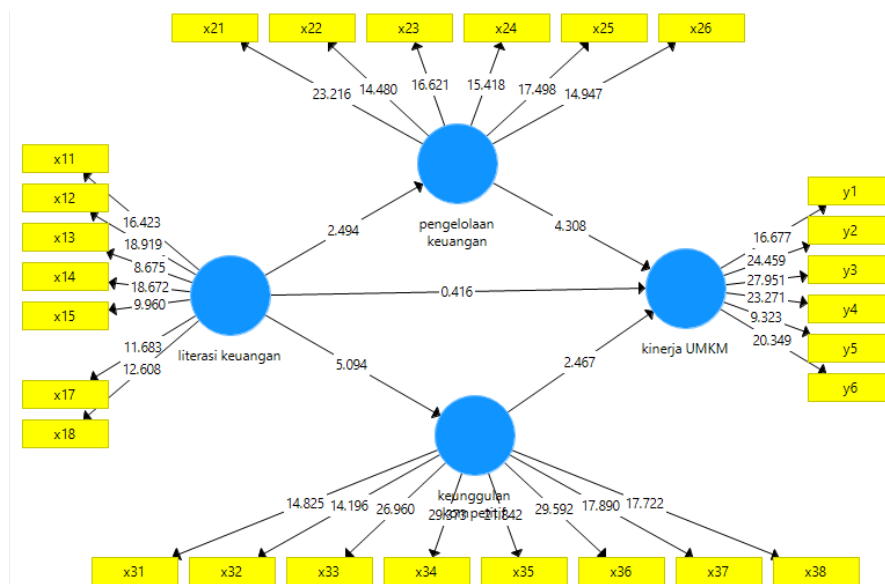


Figure 2. Output SmartPLS

Source: SmartPLS (2025)

From the analysis results in SmartPLS Software, the cross-loading values of each indicator in the Financial Literacy, Financial Management, Competitive Advantage, and Financial Performance variables are higher for their respective variable constructs than for other latent variable constructs. This indicates that each indicator in this study better reflects its respective variable than other variables, it can be concluded that the model has met the discriminant validity requirements, and all indicators have passed the discriminant validity test with cross-loading criteria. The structural inner model is an important part of the Partial Least Square Structural Equation Model (PLS-SEM) path analysis. The inner model is used to test the relationship between latent variables in a model. Figure 2 below shows the outer model results obtained using SmartPls software.

In this study, hypothesis testing was conducted using SmartPLS version 4 through a bootstrapping approach. A two-tailed bootstrapping procedure was applied with a significance level of 5% (0.05). The t-table value for a sample size of 140 respondents is 1.9661. The decision criteria state that if the T-statistic is lower than the t-table value and the P-value is less than 0.05, then  $H_0$  is accepted and  $H_a$  is rejected. Conversely, if the T-statistic exceeds the t-table value and the P-value is greater than 0.05, then  $H_0$  is rejected and  $H_1$  is accepted. The results obtained from the bootstrapping procedure are presented in Table 1.

**Table 1. Path Coefficients**

	T Statistics	P Values	Decision
Competitive Advantage→MSEMs Performance	2.467	0.014	Accepted
Financial Literacy →Competitive Advantage	4.973	0.000	Accepted
Financial Literacy→ MSEMs Performance	0.42	0.675	Rejected
Financial Literacy→ Financial Management	2.575	0.010	Accepted
Financial Management →MSEMs Performance	4.616	0.000	Accepted

Source: Authors Work (2025)

### **The Effect of Competitive Advantage on Financial Performance**

The hypothesis testing results indicate that Competitive Advantage has a positive effect on Financial Performance. This is reflected in the original sample value of 0.229, a T-statistic of 2.467 which exceeds the t-table value of 1.966, and a P-value of 0.014 which is below the 0.05 significance threshold. These findings suggest that higher levels of competitive advantage are associated with improved financial performance. Competitive advantage enables firms to outperform competitors through greater efficiency, innovation, superior product quality, and enhanced service, which ultimately contributes to better financial outcomes. Therefore, the first hypothesis in this study is supported.

### **The Effect of Financial Literacy on Competitive Advantage**

The analysis results reveal that Financial Literacy has a positive and significant effect on Competitive Advantage. This is evidenced by an original sample value of 0.374, a T-statistic of 4.973 which exceeds the critical value of 1.966, and a P-value of 0.000 which is below the 0.05 threshold. These findings indicate that higher levels of financial literacy among business actors increase their ability to develop and strengthen competitive advantage. Financial literacy enhances the capacity to

manage capital effectively, make sound investment decisions, and formulate appropriate financial strategies, thereby improving business competitiveness. Therefore, the second hypothesis in this study is supported.

### **The Effect of Financial Literacy on Financial Performance**

The findings indicate that Financial Literacy does not have a significant effect on Financial Performance. This is reflected in the original sample value of -0.044, a t-statistic of 0.420 which is below the critical value of 1.966, and a p-value of 0.675 which exceeds the 0.05 significance level. These results suggest that improvements in financial literacy do not necessarily lead to better financial performance. This may occur because, although business actors possess adequate financial knowledge, such knowledge is not always effectively translated into practical business strategies. Moreover, other factors such as market conditions, managerial capabilities, and external influences may play a more dominant role in determining financial performance. Therefore, the third hypothesis is not confirmed.

### **The Effect of Financial Literacy on Financial Management**

The analysis findings indicate that Financial Literacy has a positive and statistically significant impact on Financial Management. This conclusion is supported by the original sample coefficient of 0.286, the t- statistic of 2.575, which exceeds the critical threshold of 1.966, and the p- value of 0.010, which is below the conventional significance level of 0.05. These results imply that increased levels of financial literacy empower entrepreneurs to engage in more systematic financial planning, allocate resources more wisely, and carry out financial record-keeping and oversight with greater efficacy. These competencies play a significant role in promoting business stability and improving the quality of financial decision-making. Consequently, the fourth hypothesis proposed in this study is thus confirmed.

### **The Effect of Financial Management on Financial Performance**

Based on the findings obtained from the analysis, the relationship between Financial Management and Financial Performance shows an original sample value of 0.449, a t-statistic of 4.616 (exceeding the threshold of 1.966), and a p-value of 0.000 (which is less than the 0.05 significance level). These findings indicate that Financial Management has a positive and statistically significant impact on Financial Performance. This implies that improved financial management practices correlate with improved financial performance outcomes. Efficient financial management, which includes careful transaction documentation, diligent cash flow management, and strategic capital allocation, can improve a company's profitability and long-term survival. Consequently, the fifth hypothesis proposed in this study is confirmed.

**Table 2. Indirect Effect**

	T Statistics	P Values	Decision
FL → CA → P	1.967	0.050	Accepted
FL → FM → P	2.747	0.006	Accepted

Source: Authors Work (2025)

### **Competitive advantage as a mediating variable of the influence of financial literacy on MSME performance**

The influence of financial literacy on the performance of small and medium enterprises (SMEs) through competitive advantage can be explained through the results of the mediation analysis, which revealed a t-statistic of 1.967, exceeding the critical t-value of 1.654. The p-value obtained was 0.050, which is below the conventional threshold of 0.05. In this context, the variable representing competitive advantage functions as a full mediator, indicating that there is only an indirect relationship between the variables that produces statistically significant results. Based on the findings from the hypothesis testing, one can conclude that financial literacy influences the performance of SMEs through the mechanism of competitive advantage. As a result, it can be stated that hypothesis H6 is confirmed.

### **Financial management as a mediating variable of the effect of financial literacy on MSME performance**

The impact of financial literacy on the performance of small and medium enterprises (SMEs) through competitive advantage is evidenced by the findings of the mediation analysis, which revealed a t-statistic value of 2.747, exceeding the t-table value of 1.654. The p-value obtained was 0.006, which is less than the conventional threshold of 0.05. In this context, variables related to financial management function as full mediators, indicating that there is only an indirect relationship between the variables that produce a significant effect. Based on the results of the hypothesis examination, it can be concluded that financial literacy affects the performance of SMEs through the lens of financial management. Consequently, it can be stated that H7 is validated.

## **Discussion**

### **The effect of financial literacy on the performance of MSMEs**

This study found that financial literacy does not directly affect the financial performance of MSMEs. This means that financial literacy, or the level of understanding that business actors have of financial concepts such as capital management, budget planning, risk management, and understanding of financial instruments, does not necessarily contribute to improving business financial performance. The reason for this is that the financial knowledge possessed by MSME entrepreneurs is not fully implemented optimally in daily business management practices and the limited resources of MSMEs, both in terms of capital, access to technology, and financial administration systems that cannot be applied consistently due to time constraints, lack of mentoring training, and low discipline in financial recording and business performance evaluation. In addition, most MSMEs do not have a formal organisational structure and financial system, so that their financial knowledge is not integrated into the business decision-making process. Therefore, financial literacy has proven insufficient in directly enhancing financial performance in the absence of effective financial management practices. In the context of MSMEs in Sidoarjo, business agents exhibiting a substantial degree of financial literacy in terms of understanding and knowledge do not necessarily improve the performance of MSME businesses. In several food and beverage sectors, there are business operators who do not yet fully understand the concept of financial literacy but are already able to demonstrate simple financial management, thereby improving

business performance. This study is consistent with (Florentina *et al.*, 2024), who state that financial literacy has no effect on the financial performance of MSMEs in East Alok, Indonesia.

### **The effect of financial literacy on MSME financial management**

This investigation determined that financial literacy has a significant effect on financial management among MSME entrepreneurs. This indicates that an increase in the degree of financial literacy among micro-entrepreneurs, the better the financial management of MSMEs in the city of Sidoarjo. These findings indicate that the higher the level of understanding of MSME actors regarding basic financial concepts such as financial recording, budget planning, cash flow management, and understanding of banking and financial products, the more effective they are in managing their business finances. MSME entrepreneurs with good financial literacy tend to be able to separate their personal and business finances, prepare simple financial reports on a regular basis, manage working capital efficiently, and be better prepared to face dynamic economic conditions. Thus, improving financial literacy is a crucial factor in strengthening the resilience and sustainability of MSMEs, especially in the face of business competition and the demands of modern economic development. The findings of this study are consistent with those of a study conducted by (Dewi & Edt, 2023), which states that the better the financial literacy of business owners, the better their financial management will be.

### **The effect of financial literacy to the competitive advantage of MSMEs**

This study found that financial literacy has a significant positive effect on the competitive advantage of MSMEs in Sidoarjo. This means that the higher the level of literacy among micro-business owners, the greater the competitive advantage of MSMEs in Sidoarjo. Financial literacy equips MSME owners with an understanding of the importance of financial planning, cost efficiency and risk management, enabling their businesses to run more stably and sustainably than those of business owners with low levels of financial literacy. In addition, high financial literacy also encourages MSMEs to be more adaptive in taking advantage of economic opportunities, including access to formal financing sources such as bank loans, small business credit programmes (KUR), and digital technology-based financing (fintech). The ability of MSME actors to understand and utilise these financial instruments enables them to increase production capacity, expand marketing networks, and innovate products. Thus, they are able to create greater added value compared to their competitors. Therefore, improving financial literacy is one of the important factors in building the competitive advantage of MSMEs, both in terms of operations, marketing, and long-term business development strategies. This study is consistent with (Komang *et al.*, 2024), who state that financial literacy and intellectual capital have a positive and significant impact on the competitive advantage of MSMEs in Buleleng Regency, Bali.

### **The effect of financial management to the MSME performance**

The results derived from this research suggest that financial management has a significant positive effect on the performance of MSMEs in Sidoarjo. This means that better financial management will improve the performance of MSMEs in Sidoarjo. These findings indicate that MSME actors who implement good financial

management practices, such as regular transaction recording, accurate financial reporting, cash flow control, and budget planning, are able to maintain business stability and optimise the use of financial resources. With good financial management, MSMEs can minimise the risk of expenditure errors, prevent capital deficits, and ensure smooth business operations. This has a direct impact on increasing efficiency and effectiveness in carrying out daily business activities. Thus, the results of this study confirm that financial management is not only an administrative aspect but also an important strategy in improving the performance and sustainability of MSMEs in Sidoarjo. In the context of MSME business performance in Sidoarjo Regency, practices such as bookkeeping, cash flow planning, cost control, and risk management improve the ability of MSMEs to make investment and operational decisions that enhance business performance. Bookkeeping and reporting improve business health measurements and facilitate performance evaluation, which in turn improves access to financing and strategic decision-making. Good financial management increases the chances of obtaining credit/formal financing, thereby increasing the ability to expand or stabilise the business. This is consistent with research (Amalia *et al.*, 2025) which states that sound financial management has a positive impact on the performance of micro-enterprises in Surakarta. This is further supported by (Rahmawati & Putri, 2023), who state that financial management can improve the performance of women-led MSMEs

### **The effect of competitive advantage to the performance of MSMEs**

These findings show that competitive advantage has a positive and significant effect on the performance of MSMEs in Sidoarjo. This means that the greater the ability of MSMEs to build competitive advantage (e.g. through product quality, innovation, or service), the better their business performance, both financially and non-financially. Competitive advantage can improve MSME performance because businesses that are able to offer unique products, better quality, continuous innovation, or satisfactory service will find it easier to attract and retain customers. This has implications for increased sales, revenue growth, market share expansion, and business profitability. In addition, competitive advantage supports the efficient use of resources, thereby improving operational performance. In the context of MSMEs in Sidoarjo, various sectors such as food and beverages, handicrafts, clothing, batik, and others require competitive advantages in the form of unique products, better quality, and continuous innovation to increase sales, turnover, and business sustainability. Without competitive advantages in terms of product quality and innovation, the sustainability of MSMEs will not last long and business performance will not improve. The MSME entities located within the Sidoarjo Regency are necessitated to augment their competitive advantages to effectively confront global challenges, which include the enhancement of product and service innovation, the development of human resources and technological capabilities, as well as the expansion of marketing domains. This strategic enhancement is imperative to elevate the market value of MSMEs, thereby enabling them to compete vigorously with the influx of foreign products permeating the Indonesian industrial landscape. This is consistent with Susanti (2023), who states that competitive advantage has a positive and significant impact on the performance of SMEs in Jember Regency. This is further supported by (Hererra *et al.*, 2023) who state that competitive advantage has a direct impact on the financial performance of SMEs in Jakarta.

### **The role of financial management in mediating the influence of financial literacy on the performance of MSMEs**

The findings of this study show that financial management can be a mediating variable in the influence of financial literacy on the financial performance of MSMEs. Financial management acts as a full mediator, whereby financial literacy cannot directly influence MSME performance, but only through the variable of financial management. Financial literacy denotes the capacity of individuals engaged in commerce to comprehend, oversee, and execute proficient financial determinations. However, financial literacy alone is not sufficient to improve MSME performance if it is not accompanied by good financial management practices. This is where financial management plays a role as a mediating variable. In the context of MSMEs in Sidoarjo, it was found that the financial literacy possessed by MSME entrepreneurs not only provides an understanding of financial concepts but also encourages the ability to manage business finances more effectively. Entrepreneurs with a good level of financial literacy are able to understand the importance of recording transactions, budgeting, working capital management, and cost control. However, the benefits of financial literacy can only be optimally realised if it is implemented in good financial management practices in business operations. Furthermore, the results of this study also provide evidence that financial literacy does not have a strong direct effect on improving MSME performance if it is not accompanied by appropriate managerial actions. The concept of financial literacy necessitates the conversion into systematic financial management methodologies such as separating business and personal finances, conducting regular financial performance evaluations, and preparing financial reports as a basis for decision-making. Thus, financial management acts as a variable that bridges financial literacy and improved business performance. Micro-entrepreneurs who are able to manage their finances well will find it easier to optimise resources, improve operational efficiency, and minimise financial risks, thereby positively impacting business performance.

These findings are in line with the RBV theory, which states that a company's performance excellence is influenced by its internal capabilities, including its ability to manage financial resources. Consequently, it can be inferred that the enhancement of financial literacy will only play a substantial role in augmenting the operational efficacy of MSMEs if it is underpinned by proficient financial management methodologies. Therefore, improving financial literacy needs to be accompanied by the implementation of good financial management as a strategy to increase the competitiveness and sustainability of MSME performance. These findings provide strong theoretical support for Financial Behaviour Theory, which states that financial literacy serves as a cognitive foundation for rational financial behaviour, which ultimately influences business success. This is consistent with research (Dwijayanty *et al.*, 2025) which states that financial management behaviour plays a significant mediating role in the relationship between financial literacy and business performance.

### **The role of competitive advantage in mediating the influence of financial literacy on the performance of MSMEs**

These findings show that competitive advantage mediates the correlation between financial literacy and the performance of MSMEs in Sidoarjo. Competitive advantage acts as a full mediator, whereby financial literacy cannot directly influence

MSME performance but only through the variable of competitive advantage. Financial literacy does not necessarily improve MSME performance, but its influence works indirectly through the establishment of competitive advantage. Thus, through the variable of competitive advantage acting as a mediating variable, it is able to improve MSME performance. In the context of MSMEs in Sidoarjo, this illustrates that the financial literacy possessed by business actors not only functions as a cognitive ability to understand financial concepts, but also has strategic implications that affect business competitiveness. Financial literacy enables MSME actors to formulate financing strategies, improve cost efficiency, and manage resources optimally. Adequate understanding of financial aspects encourages business actors to make rational decisions in capital use, investment planning, and risk control. Thus, financial literacy serves as a foundation that strengthens the ability of MSMEs to build competitive advantage through increased efficiency, product innovation, and responsiveness to market needs. MSME actors with high financial literacy tend to be able to formulate differentiation strategies, whether through improving product quality, setting competitive prices, or strengthening customer service. These strategies provide added value that is recognised by consumers, thereby increasing customer loyalty and expanding market share. The competitive advantage resulting from the application of financial literacy ultimately leads to improved business performance, both in financial aspects such as increased revenue and profitability, and in non-financial aspects such as business sustainability and reputation.

These findings are in line with the RBV perspective, which states that a company's competitive advantage can be created through the utilisation of internal resources that are valuable, rare, difficult to imitate, and not easily replaced. Financial literacy is an internal capability that can strengthen a business's competitive advantage when applied effectively. Furthermore, the results of this study support previous empirical findings which state that financial literacy has an indirect relationship with business performance through the mechanism of increasing competitive advantage. Thus, it can be concluded that improving the financial literacy of MSME actors needs to be oriented not only towards knowledge, but also towards developing business strategies that can create competitive advantages as the main pathway to enhancing the efficacy of Micro, Small, and Medium Enterprises (MSMEs) in a manner that is sustainable. This is consistent with research (Hererra *et al.*, 2023) which states that competitive advantage acts as a mediating variable between financial literacy and the business performance of MSMEs in Jakarta.

The results indicate that financial literacy does not directly influence MSME performance but operates indirectly through financial management and competitive advantage as full mediators. This finding contrasts with (Santoso *et al.*, 2023) who report a direct effect, yet aligns with (Ghefira Hanifah & Innayah, 2024) suggesting that contextual and managerial mechanisms shape the literacy–performance linkage. From an RBV perspective (Barney, 1991), financial literacy constitutes an abstract cognitive asset that fails to produce performance results unless integrated within organizational competencies. In this study, financial management functions as an operational capability that translates knowledge into structured financial practices, while competitive advantage reflects the strategic manifestation of internal resources in market positioning. Thus, the findings extend RBV by demonstrating that cognitive resources influence firm performance only when transformed into managerial

routines and competitive strategies. Practically, this implies that MSME development programs should move beyond financial education and integrate structured bookkeeping implementation, cost-based pricing training, and innovation budgeting to ensure that financial literacy is converted into measurable business performance improvements.

## CONCLUSION

This study concludes that financial literacy does not directly enhance MSME performance; rather, its influence operates indirectly through financial management and competitive advantage as full mediating variables. These findings clarify the inconsistent results in prior studies by demonstrating that financial literacy functions as a foundational cognitive resource that must be transformed into structured managerial practices and strategic positioning before generating measurable performance outcomes. From a Resource-Based View (RBV) perspective, the study contributes theoretically by distinguishing between internal cognitive resources (financial literacy) and operational capabilities (financial management and competitive advantage), showing that performance advantages emerge only when knowledge is embedded into organizational routines and competitive strategies. However, this research is limited by its design and relatively narrow geographic scope, which may restrict the generalizability of the findings and the ability to capture dynamic capability development over time.

In practice, the findings imply that MSME development initiatives should move beyond financial education alone and emphasize structured financial management, including systematic bookkeeping, cash flow monitoring, cost-based pricing, and strategic resource allocation for innovation. Policymakers and MSME support institutions are encouraged to design integrated training models that combine literacy enhancement with hands-on managerial mentoring to ensure capability transformation. Researchers hope that future research will further develop the model by incorporating variables such as digital technology adoption, entrepreneurial orientation, or innovation capability to further explore how internal capabilities interact in shaping sustainable MSME performance across different regional contexts.

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