

DETERMINANTS OF FINANCIAL PERFORMANCE EVALUATION IN SMALL AND MEDIUM ENTERPRISES

Amir Hamzah^{1*}, Teti Rahmawati², Chintia Fitriani³, Yudi Febriansyah⁴

Universitas Kuningan¹²³⁴

¹Corresponding author: amir.hamzah@uniku.ac.id

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ABSTRAK

Penelitian ini menganalisis faktor-faktor yang memengaruhi kinerja keuangan Usaha Kecil dan Menengah (UKM), mengatasi minimnya penelitian yang berfokus pada variabel spesifik dalam konteks UKM. Penelitian ini mengkaji pengaruh mental accounting, pencatatan keuangan, literasi keuangan, manajemen keuangan, dan akuntansi digital terhadap kinerja keuangan UKM. Data dari 216 UKM di Kabupaten Kuningan dianalisis menggunakan Structural Equation Modeling (SEM). Hasil penelitian menunjukkan bahwa pencatatan keuangan, literasi keuangan, dan manajemen keuangan memiliki pengaruh positif yang signifikan terhadap kinerja keuangan UKM. Sebaliknya, mental accounting memiliki pengaruh negatif yang signifikan, sedangkan akuntansi digital tidak signifikan mempengaruhi kinerja keuangan. Temuan ini menunjukkan bahwa praktik pengelolaan keuangan yang efektif dapat meningkatkan kinerja keuangan, sementara penggunaan mental accounting yang tidak tepat serta implementasi akuntansi digital yang kurang optimal dapat menjadi hambatan. Penelitian ini mengimplikasikan perlunya peningkatan literasi keuangan, penerapan praktik manajemen keuangan yang lebih efektif, serta pelatihan akuntansi digital bagi UKM menghadapi tantangan keuangan.

Kata Kunci: UKM, kinerja keuangan, faktor kontekstual UKM

ABSTRACT

This study analyzes factors influencing the financial performance of small and medium enterprises (SMEs), addressing the limited research that focuses on specific variables in the SME context. It examines the effects of mental accounting, financial record-keeping, financial literacy, financial management, and digital accounting on SME financial performance. Using Structural Equation Modeling (SEM), data from 216 SMEs in Kuningan Regency were analyzed. The findings reveal that financial record-keeping, financial literacy, and financial management significantly and positively impact SME financial performance. Conversely, In contrast, mental accounting has a significant negative impact, while digital accounting does not significantly affect financial performance. These results suggest that effective financial management practices can enhance financial performance, while improper use of mental accounting and ineffective implementation of digital accounting may hinder it. This research implies the need to improve financial literacy, adopt more effective financial management practices, and provide digital accounting training to help SMEs overcome financial challenges.

Keywords: SMEs, financial performance, contextual factor of SMEs



1. Introduction

Small and Medium Enterprises (SMEs) play a crucial role in Indonesia's economy. As one of the largest contributors to the Gross Domestic Product (GDP), SMEs are also essential in creating job opportunities and ensuring economic equality across various regions in Indonesia. The presence of SMEs in sectors such as agriculture, trade, manufacturing, and creative industries drives local economic growth. However, despite their significant potential, many SMEs face serious challenges in managing their finances effectively. One of the main challenges is the low level of financial literacy and the lack of understanding of sound accounting practices, which ultimately affects their performance and sustainability.

In Indonesia, poor financial management is often the primary reason for the failure of SMEs. Many business owners still do not understand the importance of organized financial record-keeping, making it difficult to plan expenditures and revenues or to make rational business decisions (Hamzah & Suhardi, 2019). In recent decades, despite the government's efforts to promote SME growth through various policies and financing programs, many small business owners are still unable to access funding due to their inability to prepare clear and detailed financial reports. This indicates an urgent need to improve financial management quality among SMEs in Indonesia.

This situation is exacerbated in border regions like Kuningan Regency, located between West Java and Central Java. Kuningan has distinct geographical and economic characteristics compared to other regions in Indonesia, with a dominant presence of sectors such as agriculture, trade, and creative industries, mostly managed by micro and small enterprises (Martika et al., 2024). Although these sectors have significant potential to drive local economic growth, many SMEs in Kuningan face substantial financial management challenges. One prominent issue is the practice of mental accounting, where business owners often mix personal and business finances, leading to difficulty in obtaining a clear picture of their business's financial health. A survey of 100 SMEs in Kuningan revealed that 65% of business owners do not separate their personal and business funds, resulting in unclear financial planning and irrational decision-making (Hamzah & Suhendar, 2020). Another challenge faced by SMEs in Kuningan is the lack of systematic financial recording and the underuse of digital accounting technology. Proper financial management and the application of digital accounting could enhance operational efficiency and ease access to financing. Many business owners in Kuningan still rely on manual and traditional record-keeping methods, which are prone to errors, making it difficult to obtain an accurate overview of their business's financial situation.

In addition, inadequate and irregular financial record-keeping remains a significant issue. Although many business owners recognize the importance of maintaining financial records, only 30% do so regularly and according to proper standards. The lack of understanding of the importance of financial statements and financial analysis means that many SMEs in Kuningan struggle with managing their cash flow. Survey results show that 70% of SMEs do not have income statements or balance sheets, making it difficult for them to determine whether their businesses are profitable or experiencing

losses (Hamzah, 2019). The poor management of financial records is further exacerbated by the low level of financial literacy among SME owners. According to the Financial Services Authority (OJK), Indonesia's national financial literacy index was still low, at 38.03% in 2023. This figure is even lower in border regions like Kuningan, indicating that many SME owners lack an understanding of basic financial concepts such as budgeting, cash flow management, and investment. Without sufficient financial literacy, SMEs find it difficult to manage and expand their businesses effectively.

With the rise of technology, digital accounting has emerged as a promising solution to address financial record-keeping and management issues in SMEs. Digital accounting allows for the automatic recording of financial transactions, real-time report generation, and a reduction of human errors (Hamzah et al., 2023a). In Kuningan, while internet access is improving, the adoption of technology within the SME sector remains limited. A survey by the Kuningan Cooperative and SME Office in 2023 found that only 25% of SMEs had implemented digital accounting systems, while the rest still relied on manual record-keeping or did not maintain financial records at all. This gap in technology adoption highlights the untapped potential of digital accounting to improve efficiency and accuracy in financial management.

Digital accounting not only simplifies financial record-keeping but also provides additional benefits, such as easier and faster access to financial data (Mawira, 2023). With digital accounting systems, SME owners can easily track cash flows, manage expenses and income, and make more informed financial decisions based on accurate financial data. Furthermore, the use of digital tools also helps SME owners comply with tax regulations, as proper tax reporting is crucial for the sustainability of their businesses (Shi et al., 2024). Therefore, adopting digital accounting can positively impact the financial performance of SMEs in Kuningan.

However, despite the great potential of technology adoption, several barriers remain in the implementation of digital accounting among SMEs in Kuningan. One major obstacle is the lack of digital knowledge and technological skills among SME owners. According to a study by the Research and Community Service Institute at Kuningan University, 40% of SME owners reported difficulty in adopting new technologies due to limited human resources and a lack of adequate training. Therefore, support from government institutions in the form of training and mentoring is essential to help SMEs adapt to digital technologies. Improving financial literacy and increasing the adoption of digital accounting are expected to enhance the financial performance of SMEs in Kuningan. With better financial management, SMEs can reduce waste, improve operational efficiency, and increase profitability. Effective financial management will contribute to more sustainable business growth, benefiting the local economy. This study aims to evaluate the impact of mental accounting, financial record-keeping, financial management, and financial literacy on the financial performance of SMEs in Kuningan, as well as explore the role of digital accounting in improving financial management among SMEs.

This study introduces several innovations that distinguish it from previous research on SME financial management, especially in border regions like Kuningan. One key novelty of the study is its interdisciplinary approach, combining mental accounting,

traditional accounting practices, and the application of digital accounting technology. This research explores how mental accounting influences financial management practices and how digital accounting can improve these practices, a concept rarely applied in the context of border-region SMEs. Another innovative aspect of this research is its focus on SMEs in border regions, which have not been widely studied in previous research. The unique economic and social conditions in border areas present distinct challenges and opportunities for SME growth and financial management. By focusing on Kuningan Regency, this study aims to provide empirical data on the financial management challenges faced by SME owners in such regions and suggest solutions tailored to their specific needs.

The main objective of this study is to evaluate how mental accounting, financial record-keeping, financial management practices, and financial literacy influence the financial performance of SMEs in Kuningan Regency. This study also aims to assess the role of digital accounting in enhancing financial management among SMEs. By understanding how these variables interact, the research will offer insights into how SMEs can improve their financial performance through better mental accounting, enhanced financial literacy, and the adoption of digital accounting systems. This research contributes both academically and practically. Academically, it adds to the limited body of knowledge on SME financial management in border regions and introduces a new framework that integrates mental accounting with digital accounting technology. Practically, the findings can help policymakers, industry practitioners, and SME owners in Kuningan by providing actionable recommendations to improve financial management practices, leading to enhanced business performance. The study also aims to inform future policies aimed at increasing digital literacy and promoting financial literacy programs for SMEs in border regions.

Several studies have investigated financial management practices in SMEs across various contexts, emphasizing the importance of financial literacy, mental accounting, and technological adoption. Hamzah & Suhardi (2019b) found that financial literacy enhances SMEs' decision-making and credit access in Malaysia, while Loko & Yang (2022) highlighted how low financial literacy impedes SME growth in South Africa, particularly in rural areas. In India, Gerrans et al., (2022) revealed that mental accounting practices significantly impact resource allocation and profitability. Lim et al., 2021) identified poor financial management as a critical barrier to SME sustainability in developing nations, and Alfianto & Nugroho (2020) demonstrated that adopting digital accounting improves financial transparency and performance globally, despite technological literacy challenges. However, research integrating mental accounting, financial literacy, record-keeping, and digital accounting in border-region SMEs remains scarce.

This study addresses the critical challenges SMEs face in Kuningan Regency, a border region where businesses struggle with financial literacy and digital technology adoption. These issues are exacerbated by reliance on informal financial practices, such as mental accounting, which hinders rational decision-making. Understanding these dynamics is essential as SMEs significantly contribute to local economies. Furthermore, the increasing emphasis on digital transformation by policymakers underscores the need

for timely research exploring the enablers and barriers to adopting digital accounting systems.

This research fills important gaps in the literature. First, it integrates mental accounting and digital accounting within a single framework, providing a novel perspective on SME financial management. Second, it focuses on border-region SMEs, a demographic often overlooked in previous studies. Finally, it examines digital accounting as a moderating variable, offering insights into its potential to improve financial practices.

The urgency of this research lies in its potential to address the practical challenges SMEs face in achieving financial sustainability, particularly in underrepresented areas like Kuningan. Improving SME financial management directly impacts economic resilience, business sustainability, and regional competitiveness. Moreover, this study aligns with Indonesia's policy priorities of promoting financial literacy and digital transformation among SMEs.

This research contributes to the literature by providing a comprehensive framework that integrates behavioral, managerial, and technological aspects of financial management. Practically, it equips SME owners with actionable strategies to enhance financial practices through better mental accounting, financial literacy, and technology adoption. Additionally, it offers policymakers evidence-based recommendations to design targeted interventions, such as digital literacy programs and financial management training. By bridging gaps in academic knowledge and addressing practical and regulatory needs, this study supports sustainable economic growth in border regions like Kuningan.

2. Theoretical Framework and Hypothesis Development

The theoretical foundation for this study is based on Agency Theory, which is commonly used to explain the relationship between business owners (principals) and managers (agents) (Kiptum, 2019). In the context of Small and Medium Enterprises (SMEs), Agency Theory emphasizes the importance of monitoring and control mechanisms to reduce conflicts of interest between owners and managers, especially when resources are limited and business decisions become complex. Agency Theory suggests that efficient financial practices, such as mental accounting, financial record-keeping, financial literacy, financial management, and digital accounting, are crucial for improving business performance and ensuring the sustainability of SMEs.

Mental accounting specifically pertains to how business owners mentally allocate and categorize their finances, including the separation of personal and business funds. While it is rational to manage finances holistically, SME owners often make decisions based on subjective and sometimes irrational categorizations. For example, owners who mix personal and business funds may inadvertently use business resources for personal expenses, compromising the financial stability of their enterprises. Such practices can result in poor financial decision-making, unclear financial records, and difficulties in evaluating the financial health of the business. These challenges ultimately affect the overall performance and sustainability of SMEs. Ineffective mental accounting is therefore expected to have a negative impact on the financial performance of SMEs.

This finding aligns with previous research, such as that by Martika et al. (2024)), which emphasized the detrimental effects of poor mental accounting on SME financial performance. Martika's study underlined the need for better financial discipline and structured approaches to separate personal and business finances as a means to enhance decision-making and improve business outcomes. By integrating the principles of Agency Theory, this study not only underscores the importance of financial practices but also explores the moderating role of digital accounting in addressing challenges like mental accounting. The adoption of digital accounting systems can help SMEs establish clearer financial boundaries, enhance record-keeping accuracy, and support better financial decision-making processes. This, in turn, contributes to improved business performance and sustainability. This study is also in line with the research conducted by Adae et al. (2021), Lai et al. (2023), Kaili et al. (2019), and Naysary et al. (2021).

H₁: Mental accounting negatively impacts the financial performance of SMEs.

Maintaining accurate financial records is critical for business owners to effectively monitor revenues, expenditures, and overall financial health. This practice supports efficient cash flow management, reduces the risk of unnecessary financial losses, and provides a foundation for sound business operations. Research by Wiharno et al. (2022) emphasizes that proper financial record-keeping enables businesses to analyze performance metrics and gain a clearer understanding of their financial standing. SMEs that adopt disciplined record-keeping practices can track financial trends, identify areas requiring improvement, and develop targeted strategies to enhance business operations. Moreover, sound financial record-keeping facilitates informed decision-making and long-term strategic planning. According to studies by Dhami & Hajimoladarvish (2020), Jiang et al. (2024), and Shahana et al. (2023) SMEs with robust financial record-keeping systems are better equipped to evaluate profitability, manage operational costs, and access external funding. These benefits directly contribute to improved financial performance and business sustainability.

H₂: Financial record-keeping positively influences the financial performance of SMEs.

Financial literacy encompasses the ability to understand and apply essential financial concepts such as budgeting, saving, and investing. SME owners with strong financial literacy are better positioned to make informed, rational financial decisions, enabling them to effectively allocate resources, manage risks, and support business growth. According to Lusardi & Messy (2023), financially literate business owners are more adept at utilizing financial tools, such as loans and investments, to drive business expansion and maintain financial stability. These capabilities are crucial for navigating the complexities of business operations and ensuring long-term sustainability. Research by Eniola & Iwu (2022), Akbaş & Seedsman (2024), and Carton et al. (2022) further supports the notion that higher financial literacy directly correlates with improved business outcomes. SME owners with enhanced financial knowledge are more likely to implement efficient financial practices, such as accurate record-keeping and effective cash flow management, resulting in better financial performance. Consequently, it is anticipated that greater financial literacy positively influences the financial performance of SMEs.

H₃: Financial literacy positively affects the financial performance of SMEs.

Good financial management practices, such as budgeting, controlling cash flow, and making informed investment decisions, are essential for the success and sustainability of any business. For SMEs, effective management of financial resources allows for optimized revenue generation, reduction of unnecessary costs, and maintenance of a stable financial position. According to Orobio et al. (2020), robust financial management practices not only help businesses operate efficiently but also contribute significantly to their long-term stability and growth.

For SMEs, adopting sound financial management strategies is expected to enhance their financial performance by enabling higher profits and fostering a stronger market presence. Studies by Mousavi & Rasaeimanesh (2023) and Dhami & Hajimoladavarish (2020) highlight that businesses with disciplined financial management are better equipped to face economic challenges, invest strategically, and maintain profitability. As a result, SMEs that implement effective financial management practices are more likely to achieve sustainable growth and a competitive advantage in the market.

H₄: Financial management positively influences the financial performance of SMEs.

Digital accounting involves leveraging technology and software to manage financial transactions and records more efficiently. By automating financial processes, SME owners can access real-time data, reducing their dependence on manual record-keeping and minimizing errors in financial reporting. Prempeh et al. (2022) emphasize that digital accounting not only enhances the accuracy of financial data but also increases transparency and operational efficiency. This shift towards digital tools allows SMEs to monitor their financial performance more effectively, leading to better-informed decision-making. The adoption of digital accounting is expected to have a positive impact on the financial performance of SMEs by improving the organization and precision of financial management. Studies by Nguyen et al. (2023) and Mutanga et al. (2021) support this claim, highlighting that digital accounting tools facilitate accurate financial reporting, streamline processes, and enable quicker adjustments to business strategies. Consequently, SMEs that embrace digital accounting are likely to experience improved financial outcomes and greater business sustainability.

H₅: Digital accounting positively affects the financial performance of SMEs.

3. Research Method

This study adopts a quantitative approach with a descriptive and causal design, aiming to analyze the factors influencing the financial performance of SMEs in the border area of Kuningan Regency. The population in this study consists of all SMEs operating in the border regions of Kuningan Regency, with a sample size of 216 SMEs selected through proportional random sampling. The respondents of this study are the owners or managers of SMEs operating in sectors such as trade, industry, and services, who provide information related to mental accounting, financial record-keeping, financial literacy, financial management, and the application of digital accounting.

Table 1. Variables Measurement

No.	Variables	Indicator	References
1	Endogen: Financial Performance	1. Business profitability (FP1) 2. Revenue Growth (FP2) 3. Business Sustainability (FP3)	(Wiharno et al., 2022)
2	Exogen: Mental Accounting	1. Personal funds mixed with business funds (MA1) 2. Lack of planning for future financial needs (MA2) 3. Inaccurate perception of financial standing (MA3)	(Abdullahi et al., 2021)
3	Financial keeping	Record- 1. Regular preparation of income statements (FRK1) 2. Regular preparation of balance sheets (FRK2) 3. Proper categorization of financial transactions (FRK3)	(Lai et al., 2023)
4	Financial Literacy	1. Knowledge of budgeting and financial planning (FL1) 2. Understanding of financial statements (FL2) 3. Ability to make informed financial decisions (FL3)	(Hamzah & Suhardi, 2019b)
5	Financial Management	1. Cash flow management (FM1) 2. Cost control practices (FM2) 3. Investment decision-making (FM3)	(Nurhayati et al., 2022)
6	Digital Accounting	1. Use of digital tools for financial record-keeping (DA1) 2. Real-time financial data tracking (DA2) 3. Automated generation of financial reports (DA3)	(Hamzah et al., 2023a)

Data were collected using a questionnaire designed to measure the variables in this study: mental accounting, financial record-keeping, financial literacy, financial management, digital accounting, and the financial performance of SMEs. The questionnaire used a 5-point Likert scale to measure respondents' perceptions of each indicator. Before data collection, the questionnaire was tested for validity and reliability to ensure that the research instrument would yield accurate and consistent data.

The research model employs Structural Equation Modeling (SEM) with the SMARTPLS software. SMARTPLS was chosen due to its ability to handle non-normally distributed data and test complex relationships between variables. The analysis is carried out in two stages: first, a measurement model test to ensure the validity and reliability of the indicators, followed by a structural model test to examine the

relationships between variables and their impact on the financial performance of SMEs in Kuningan Regency.

Here is the mathematical equation for the outer model and inner model in this study:

1. Outer Model

The outer model specifies the relationship between the latent variables and their corresponding indicators (observable variables). It defines how the measured indicators are associated with their respective latent constructs.

The relationship between each exogenous latent variable and its indicators is modeled as follows:

$$X = \Lambda_Z \xi + \delta$$

For the endogenous latent variables, the equation is as follows:

$$y = \Lambda_y \eta + \zeta$$

a. Mental Accounting (MA)

$$MA_1 = \lambda_{MA1} \cdot MA + \varepsilon_{MA1}$$

$$MA_2 = \lambda_{MA2} \cdot MA + \varepsilon_{MA2}$$

$$MA_3 = \lambda_{MA3} \cdot MA + \varepsilon_{MA3}$$

b. Financial Record keeping (FRK)

$$FRK_1 = \lambda_{FRK1} \cdot FRK + \varepsilon_{FRK1}$$

$$FRK_2 = \lambda_{FRK2} \cdot FRK + \varepsilon_{FRK2}$$

$$FRK_3 = \lambda_{FRK3} \cdot FRK + \varepsilon_{FRK3}$$

c. Financial Literacy (FL)

$$FL_1 = \lambda_{FL1} \cdot FL + \varepsilon_{FL1}$$

$$FL_2 = \lambda_{FL2} \cdot FL + \varepsilon_{FL2}$$

$$FL_3 = \lambda_{FL3} \cdot FL + \varepsilon_{FL3}$$

d. Financial Management (FM)

$$FM_1 = \lambda_{FM1} \cdot FM + \varepsilon_{FM1}$$

$$FM_2 = \lambda_{FM2} \cdot FM + \varepsilon_{FM2}$$

$$FM_3 = \lambda_{FM3} \cdot FM + \varepsilon_{FM3}$$

e. Digital Accounting (DA)

$$DA_1 = \lambda_{DA1} \cdot DA + \varepsilon_{DA1}$$

$$DA_2 = \lambda_{DA2} \cdot DA + \varepsilon_{DA2}$$

$$DA_3 = \lambda_{DA3} \cdot DA + \varepsilon_{DA3}$$

2. Inner Model

The inner model specifies the relationships between endogenous and exogenous latent variables. The endogenous latent variables in this study are financial performance dimensions, such as business profitability, revenue growth, and business sustainability. The exogenous latent variables include mental accounting, financial record-keeping, financial literacy, financial management, and digital accounting.

The general structural equation for the inner model is expressed as follows:

$$\eta = \beta_\eta + \Gamma_\xi + \zeta$$

The equation for the inner model :

1. Business Profitability (FP1)

$$FP1 = \beta_{MA} \cdot MA + \beta_{FRK} \cdot FRK + \beta_{FL} \cdot FL + \beta_{FL} \cdot FL + \beta_{FM} \cdot FM + \beta_{DA} \cdot DA + \zeta_1$$

2. Revenue Growth (FP2)

$$FP2 = \beta_{MA} \cdot MA + \beta_{FRK} \cdot FRK + \beta_{FL} \cdot FL + \beta_{FL} \cdot FL + \beta_{FM} \cdot FM + \beta_{DA} \cdot DA + \zeta_2$$

3. Business Sustainability (F3)

$$FP3 = \beta_{MA} \cdot MA + \beta_{FRK} \cdot FRK + \beta_{FL} \cdot FL + \beta_{FL} \cdot FL + \beta_{FM} \cdot FM + \beta_{DA} \cdot DA + \zeta_3$$

The analysis technique used in this study is path analysis to test the proposed hypotheses. The results from this analysis will reveal the extent to which mental accounting, financial record-keeping, financial literacy, financial management, and digital accounting affect the financial performance of SMEs in the border areas. This research is expected to provide valuable insights into improving financial management practices in SMEs, particularly in border regions, to support local economic growth.

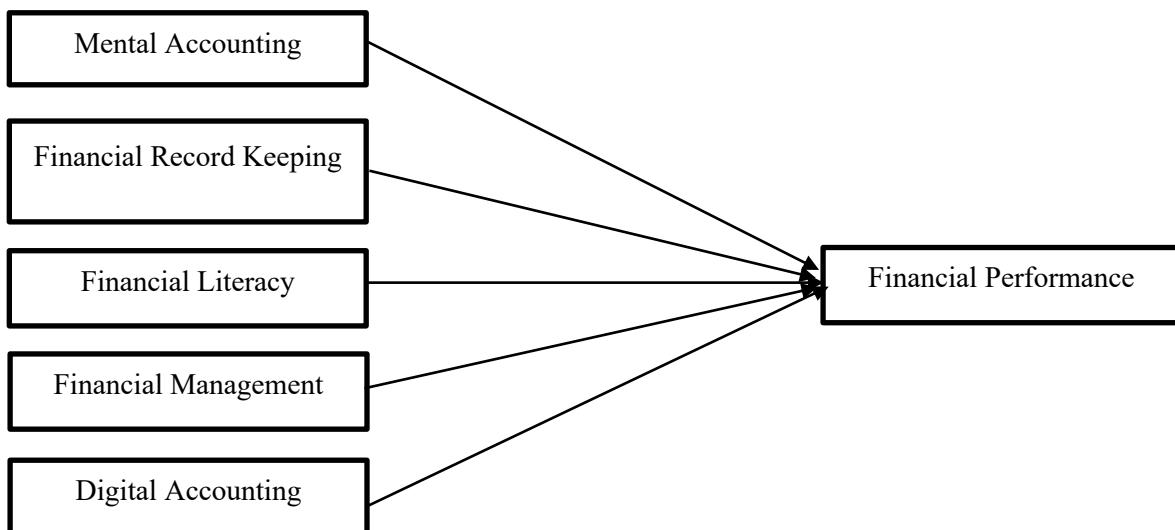


Figure 1. Research model

4. Result and Discussion

The table below outlines the demographic characteristics of respondents in this study, focusing on SMEs in Kuningan's border region. Respondents, SME owners or managers, provided insights into their business practices and financial performance. These demographic factors, such as age, gender, education, business experience, and use of digital accounting tools, are essential for understanding the context of the participants and interpreting the financial performance of SMEs in the area.

Table 2. Characteristics of Respondents

Variables	Categories	Frequency	Percentage (%)
Age	18-30 years	50	23.10%
	31-40 years	70	32.40%
	41-50 years	60	27.80%
	51+ years	36	16.70%
Gender	Male	120	55.60%
	Female	96	44.40%
Level of Education	Elementary School (SD)	30	13.89%
	Junior High School (SMP)	80	37.04%
	Senior High School (SMA)	60	27.78%
	Bachelor's Degree (S1)	46	21.30%
Business Experience	0-5 years	72	33.30%
	6-10 years	84	38.90%
	11-15 years	42	19.40%
	16+ years	18	8.30%
Use of Digital Tools	Yes (Uses digital accounting tools)	96	44.40%
	No (Does not use digital accounting tools)	120	55.60%

Source: Processed data, 2024

The respondents in this study are characterized by various demographic and business-related factors, as shown in Table 2. In terms of age, the largest group is between 31-40 years (32.40%), followed by the 41-50 years group (27.80%). Respondents aged 18-30 years make up 23.10%, while those aged 51 and above represent 16.70%. Regarding gender, the majority of respondents are male (55.60%), while 44.40% are female. In terms of education, the highest proportion of respondents have completed Junior High School (SMP) (37.04%), followed by Senior High School (SMA) graduates (27.78%). Bachelor's degree holders (S1) represent 21.30%, and 13.89% have only completed Elementary School (SD). For business experience, the majority (38.90%) have 6-10 years of experience, followed by those with 0-5 years (33.30%). Respondents with 11-15 years of business experience represent 19.40%, and those with 16 or more years of experience make up 8.30%. Lastly, regarding the use of digital tools, 44.40% of the respondents use digital accounting tools, while 55.60% do not. This comprehensive profile of respondents helps contextualize the study's findings in terms of their age, education, business experience, and technological adoption.

Based on the analysis of the Tolerance and Variance Inflation Factor (VIF) values in Table 3, it can be concluded that there are no significant multicollinearity issues in the model. All VIF values are below 5, indicating that the correlation between variables is not too high and is acceptable for regression analysis. Additionally, the Tolerance values above 0.5 for each variable further support this conclusion, as higher Tolerance values indicate lower chances of multicollinearity between variables. Therefore, the

regression model can be considered valid for further analysis without concerns about multicollinearity.

Table 3. Multicollinearity Test Results

Variable	Tolerance	VIF
Mental Accounting	0,571	1,888
Financial Record Keeping	0,590	1,821
Financial Literacy	0,601	1,901
Financial Management	0,630	1,910
Digital Accounting	0,666	1,999
Financial Performance	0,705	1,862

Source: Processed data, 2024

Table 4. Results of Validity and Reliability Analysis

Construct	Item	Loading	Alpha	rho_A	CR	AVE
Mental Accounting	MA1	0,985				
	MA2	0,975	0,983	0,984	0,989	0,967
	MA3	0,990				
Financial Record Keeping	FRK1	0,934				
	FRK2	0,959	0,929	0,937	0,954	0,875
	FRK3	0,912				
Financial Literacy	FL1	0,975				
	FL2	0,972	0,964	0,965	0,977	0,933
	FL3	0,951				
Financial Management	FM1	0,860				
	FM2	0,890	0,863	0,875	0,916	0,784
	FM3	0,905				
Digital Accounting	DA1	0,950				
	DA2	0,930	0,942	0,952	0,963	0,896
	DA3	0,956				
Financial Performance	FP1	0,939				
	FP2	0,856	0,863	0,868	0,917	0,786
	FP3	0,863				

Source: Processed data, 2024

Based on the findings presented in Table 4 the results of validity and reliability analysis, it can be concluded that the majority of the constructs exhibit strong validity and reliability. For the Mental Accounting (MA) construct, the item loadings (MA1, MA2, MA3) are exceptionally high, ranging from 0.975 to 0.990, reflecting excellent convergent validity. The reliability indicators, including Cronbach's alpha (0.983), rho_A (0.984), Composite Reliability (CR, 0.989), and Average Variance Extracted (AVE, 0.967), all exceed the acceptable thresholds, confirming both the validity and reliability of this construct. The Financial Record Keeping (FRK) construct also shows strong item loadings (FRK1, FRK2, FRK3), ranging from 0.912 to 0.959, and reliability

measures, such as Cronbach's alpha (0.929), rho_A (0.937), CR (0.954), and AVE (0.875), indicate high reliability and validity. Similarly, Financial Literacy (FL) demonstrates excellent results, with item loadings (FL1, FL2, FL3) between 0.951 and 0.975, and strong reliability indicators (alpha = 0.964, rho_A = 0.965, CR = 0.977, AVE = 0.933).

Financial Management (FM), although the item loadings (FM1, FM2, FM3) range from 0.860 to 0.905, which is slightly lower than other constructs, the reliability measures, including Cronbach's alpha (0.863), rho_A (0.875), CR (0.916), and AVE (0.784), still indicate acceptable reliability. In the case of Digital Accounting (DA), the item loadings (DA1, DA2, DA3) are robust, ranging from 0.930 to 0.956, with excellent reliability indicators (alpha = 0.942, rho_A = 0.952, CR = 0.963, AVE = 0.896). Lastly, the Financial Performance (FP) construct shows good convergent validity, with item loadings (FP1, FP2, FP3) ranging from 0.856 to 0.939. However, the reliability indicators (alpha = 0.863, rho_A = 0.868, CR = 0.917, AVE = 0.786) suggest slightly lower reliability compared to the other constructs. Overall, most constructs show strong validity and reliability, making this measurement model suitable for further analysis.

Table 5. Discriminant Validity and Discriminant Validity (HTMT)

Discriminant Validity						
	MA	FRK	FL	FM	DA	FP
MA	0,984					
FRK	0,877	0,935				
FL	0,606	0,577	0,966			
FM	0,472	0,465	0,745	0,885		
DA	0,365	0,384	0,602	0,944	0,946	
FP	0,741	0,819	0,846	0,675	0,546	0,887

Discriminant Validity (HTMT)						
	MA	FRK	FL	FM	DA	FP
MA	0,627					
FRK	0,603	0,802				
FL	0,593	0,612	0,758			
FM	0,399	0,604	0,509	0,817		
DA	0,373	0,621	0,503	0,804	0,888	
FP	0,450	0,666	0,501	0,810	0,781	0,810

Source: Processed data, 2024

Based on the results presented in Table 5 discriminant validity shows that each construct has a higher square root of Average Variance Extracted (AVE) than its correlations with other constructs, indicating strong discriminant validity. For example, the value for Mental Accounting (0.984) is higher than its correlations with other constructs, such as Financial Record Keeping (0.877) and Financial Literacy (0.606). This pattern is consistent across all constructs, confirming that they are distinct and measure different concepts without high correlations. Based on the results presented in Table 5 Discriminant Validity (HTMT) shows that all HTMT values are below the

recommended threshold of 0.85, indicating good discriminant validity. For example, the HTMT value between Mental Accounting (MA) and Financial Record Keeping (FRK) is 0.627, and between Digital Accounting (DA) and Financial Performance (FP) is 0.781, confirming that the constructs are distinct and measure different dimensions.

Table 6. Summary of Structural Equation Modelling Analysis

Hypothesis/ Direct Relationship	Predicted Sign	Beta/Coefficient	t-value	p-value Sign.	Findings
H1: MA → FP	-	-0,169	2,233	0,028	Supported
H2: FRK → FP	+	0,625	9,689	0,000	Supported
H3: FL → FP	+	0,501	6,949	0,000	Supported
H4: FM → FP	+	0,263	2,763	0,007	Supported
H5: DA → FP	+	-0,183	3,057	0,003	Supported

R Square	= 0,888
Adj. R Square	= 0,884
Effect Size:	
Mental Accounting	= 0,611 (Large)
Financial Record Keeping	= 0,590 (Large)
Financial Literacy	= 0,512 (Large)
Financial Management	= 0,580 (Large)
Digital Accounting	= 0,110 (Small)
Predictive Value Relevant	= 0,811

Source: Processed data, 2024

Based on the results of the bootstrapping test presented in Table 6, several important conclusions can be drawn regarding the factors influencing the financial performance of SMEs. Firstly, Hypothesis 1 (H1), which examines the relationship between mental accounting and financial performance, reveals a significant negative effect (Beta = -0.169, T = 2.233, P = 0.028). This indicates that higher usage of mental accounting, where business owners mentally separate personal and business finances in an irrational manner, tends to negatively affect financial performance. As a result, the hypothesis is supported, suggesting that reducing reliance on mental accounting could lead to improved financial performance for SMEs. Secondly, Hypothesis 2 (H2), which looks at the impact of financial record-keeping on financial performance, shows a significant positive effect (Beta = 0.625, T = 9.689, P = 0.000). This indicates that better financial record-keeping practices significantly enhance financial performance. The findings support the hypothesis and underscore the critical role of maintaining accurate and organized financial records, which enable businesses to make informed decisions and improve their financial stability.

Thirdly, Hypothesis 3 (H3), which investigates the effect of financial literacy on financial performance, also shows a significant positive effect (Beta = 0.501, T = 6.949, P = 0.000). This result suggests that higher financial literacy among business owners leads to better financial decision-making, which positively influences financial

performance. The hypothesis is supported, highlighting the importance of financial education for SMEs to improve their financial outcomes. In addition, Hypothesis 4 (H4), which explores the relationship between financial management practices and financial performance, shows a significant positive effect (Beta = 0.263, T = 2.763, P = 0.007). This indicates that good financial management, including practices such as budgeting, cash flow management, and cost control, positively impacts financial performance. The hypothesis is supported, confirming that effective financial management is crucial for enhancing the financial performance of SMEs. Lastly, Hypothesis 5 (H5), which examines the effect of digital accounting on financial performance, shows a significant negative effect (Beta = -0.183, T = 3.057, P = 0.003). This indicates that the use of digital accounting does not positively influence financial performance, suggesting that despite its expected benefits in improving financial management, improper or ineffective implementation of digital accounting may decrease financial performance.

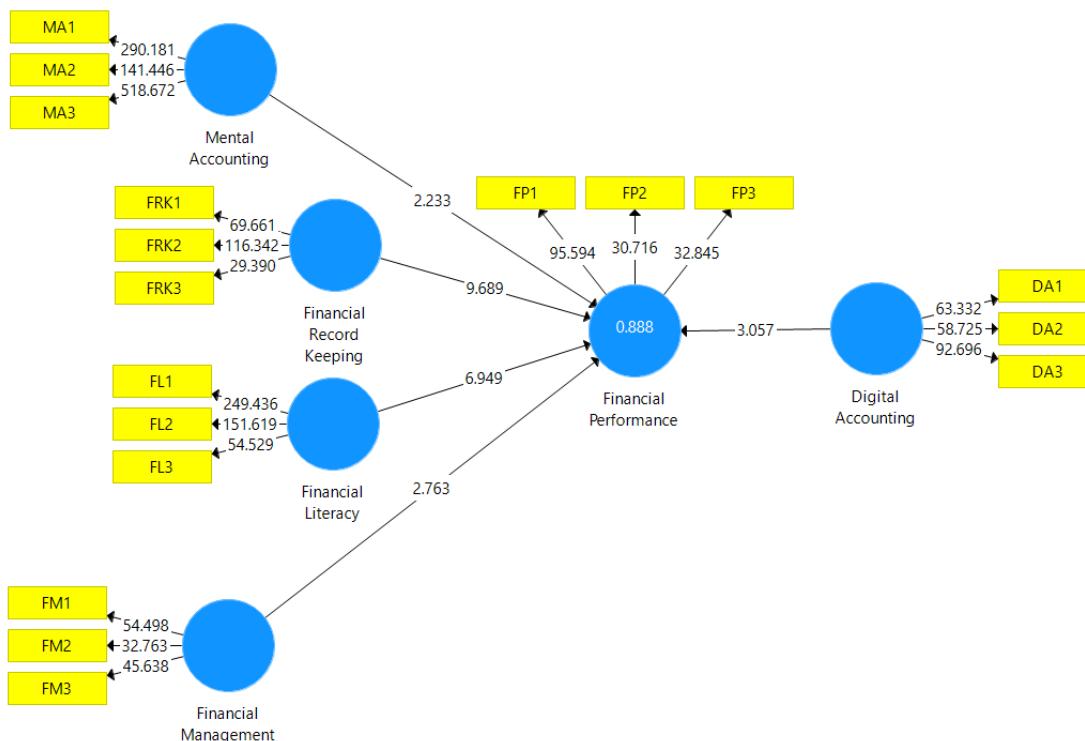


Figure 2. Measurement Model and Structural Model

Based on the R Square and Adjusted R Square values for Financial Performance (0.888 and 0.884, respectively), it can be concluded that approximately 88.8% of the variance in financial performance is explained by the model. The adjusted R Square value of 0.884 suggests that the model remains robust even after accounting for the number of predictors included. This indicates a strong fit of the model in explaining financial performance. Based on the effect size values, it can be concluded that mental accounting (0.611), financial record keeping (0.590), financial literacy (0.512), and

financial management (0.580) all have a large and significant impact on financial performance, highlighting the importance of sound financial practices and understanding. In contrast, digital accounting (0.110) shows a smaller effect on financial performance, suggesting that while it offers efficiency, its direct impact is less pronounced compared to other variables. These results emphasize the importance of integrating financial knowledge and management for improving financial outcomes. Based on the Q^2 value presented in Table 6, the predictive relevance for financial performance is 0.811. This indicates that the model has a strong predictive ability, with 81.1% of the variance in financial performance being explained by the variables included in the model. A Q^2 value greater than 0.35 suggests a good predictive relevance, and this result confirms that the model provides reliable predictions regarding financial performance.

Mental accounting refers to the way individuals mentally categorize and manage their finances, often irrationally, such as separating personal and business funds even though, logically, they should be managed together. In the context of small and medium enterprises (SMEs), this practice can lead to ineffective financial management, such as using business funds for personal expenses or failing to maintain clear financial records between personal and business finances. The findings of this study indicate that the higher the reliance on mental accounting, the lower the financial performance of SMEs. This is because mental accounting encourages disorganized financial decisions that are not based on accurate data. When business owners fail to separate personal and business expenses, it affects their ability to plan and manage cash flows and allocate resources optimally. This practice can also lead to errors in decision-making, which ultimately negatively impacts the profitability and financial stability of the business. This finding is supported by Vinogradova & Kalinina (2022), who argue that mental accounting causes business owners to make financial decisions based on cognitive biases rather than precise financial data, impairing their ability to make informed financial decisions. Similarly, Mutanga et al. (2021) highlight that the irrational allocation of resources, as seen in mental accounting practices, significantly undermines business profitability, especially in SMEs with limited resources. Vyas & Jain (2020) further support this notion, noting that mental accounting prevents SMEs from having a comprehensive view of their financial status, affecting long-term financial sustainability. Swacha-Lech & Solarz (2019) also emphasize that failing to properly manage personal and business finances can lead to missed growth opportunities and unnecessary financial stress for business owners. Reducing reliance on mental accounting can help SME owners improve their financial performance. This would involve adopting a more rational approach to financial management, including the proper separation of personal and business finances and the use of systematic, structured bookkeeping. Such practices ensure that financial decisions are based on accurate data, leading to more informed, strategic decisions that will ultimately improve financial performance in the long run. Therefore, this study suggests that encouraging SME owners to adopt more rational and structured financial management approaches could significantly improve their financial outcomes. Additionally, SME owners should be educated on the importance of clear

financial record-keeping and the negative implications of mental accounting on their business's financial health.

Financial record keeping plays a crucial role in enhancing financial performance by enabling individuals or organizations to efficiently track and manage their financial resources. Accurate and comprehensive records of income, expenses, and other financial transactions provide the foundation for making informed decisions, identifying inefficiencies, and planning for future financial objectives. This practice boosts financial transparency, improving budgeting, forecasting, and overall management, all of which are critical for achieving strong financial results. Furthermore, proper record-keeping reduces the likelihood of mistakes or oversights that could lead to financial mismanagement, thereby positively influencing financial performance. From the perspective of agency theory, the positive relationship between financial record keeping and financial performance can be better understood. In agency theory, principals (e.g., business owners or investors) entrust agents (e.g., managers or employees) with financial decision-making. These agents typically have more detailed financial knowledge, but due to information asymmetry, they may act in their interests rather than those of the principals. By maintaining detailed and transparent financial records, this information imbalance is reduced, allowing principals to monitor and assess the agents' financial actions. Such openness fosters trust and ensures that agents' decisions are more likely to align with the principal's goals, leading to improved financial management and better performance.

This perspective aligns with the findings of several studies. Coda (2020) notes that transparency in financial record-keeping improves the relationship between principals and agents, enabling more efficient financial management. Espinosa-Méndez & Correa (2022) argue that clear financial documentation helps businesses avoid financial mismanagement by providing a reliable basis for decision-making. Narh (2022) further emphasizes that effective financial record-keeping helps organizations identify inefficiencies and make timely corrective actions, ultimately boosting financial performance. Ng'ora et al.(2022) reinforce this, highlighting how systematic record-keeping enhances accountability and reduces the risk of financial discrepancies, leading to stronger financial outcomes. In conclusion, the findings of this study reinforce the importance of financial record-keeping as a key driver of financial performance. By enabling better decision-making, enhancing transparency, and mitigating the risks of financial mismanagement, proper record keeping supports the achievement of stronger financial results for SMEs.

Financial literacy plays a significant role in improving financial performance, as it equips individuals and organizations with the necessary knowledge and skills to make informed financial decisions. Individuals with higher levels of financial literacy are better at understanding key financial concepts such as budgeting, saving, investing, and managing debt, which directly enhances their ability to optimize financial resources. Financially literate individuals or managers are more likely to avoid poor financial practices, make informed investment choices, and plan effectively for long-term financial goals, all of which lead to improved financial performance. With a better

understanding of financial principles, they can manage their finances more efficiently, reduce financial risks, and increase overall wealth and profitability.

In the context of agency theory, the positive effect of financial literacy on financial performance can be explained through the interaction between principals and agents. Agency theory posits that principals, such as investors or business owners, delegate financial management to agents, like managers or employees, who typically possess more detailed financial knowledge. However, if agents lack financial literacy, they may make decisions that do not align with the principal's objectives, leading to suboptimal financial outcomes. By promoting financial literacy, agents are better equipped to understand the consequences of their decisions and align them with the goals of the principal. Financially literate agents are less likely to engage in risky or inefficient financial practices, thus reducing agency problems and improving financial outcomes for both parties. This aligns with the research conducted by Kim et al. (2021) who emphasized the importance of financial literacy in improving decision-making and organizational performance. Adela et al. (2024) also highlighted that financial literacy helps bridge the gap between principals and agents, ensuring better alignment of financial strategies. Similarly, Hasibuan & Hardana (2024) argued that financial literacy strengthens financial decision-making capabilities, leading to enhanced financial stability. Furthermore, Asikhia & Naidoo (2020) reinforced the notion that financial literacy reduces agency issues by promoting better financial practices and decision-making. In conclusion, financial literacy is a key driver of financial performance. By improving financial knowledge and decision-making, both agents and principals can achieve better financial outcomes. Promoting financial literacy within an organization or among individuals helps reduce agency problems, enhances decision-making, and ultimately leads to improved financial performance.

Financial management has a crucial positive effect on financial performance, as it encompasses the strategic planning, organization, direction, and control of financial resources to achieve an organization's objectives. Effective financial management ensures efficient resource allocation, cost control, and alignment of investment decisions with long-term goals, leading to improved cash flow, profitability, and overall financial stability. Key practices such as budgeting, forecasting, and financial analysis enable businesses to make data-driven decisions, minimize financial risks, and maximize returns. Organizations with strong financial management practices are thus better positioned for sustainable growth and strong financial performance. In the context of agency theory, the positive impact of financial management on financial performance can be understood through the interaction between principals and agents. Agency theory suggests that principals, such as business owners or shareholders, delegate financial decision-making to agents, like managers, who typically have greater expertise in financial matters. However, due to information asymmetry and potentially conflicting interests, agents may make decisions that do not align with the principals' objectives. Effective financial management mitigates this agency problem by ensuring optimal use of financial resources, thus aligning the interests of both parties. When agents adopt sound financial management practices, such as strategic planning, budgeting, and risk management, they are more likely to make decisions that benefit the principal,

improving financial performance. By promoting transparency, accountability, and alignment of financial goals, good financial management helps reduce opportunistic behavior, ultimately fostering better financial outcomes for both agents and principals. This aligns with the research conducted by Alsedrah (2023), who emphasized the importance of financial management in ensuring optimal resource utilization and improving performance. Huang et al. (2022) also discussed how effective financial management practices help organizations make informed financial decisions, leading to enhanced profitability and stability. Similarly, Hamzah & Nopiyanti (2024) highlighted that sound financial management reduces agency issues by aligning the interests of both principals and agents. Apriyanti & Budiman (2023) further supported the notion that financial management ensures efficient decision-making and fosters better financial outcomes by aligning the goals of agents and principals. In conclusion, effective financial management plays a vital role in improving financial performance by ensuring that resources are utilized efficiently, and financial decisions align with long-term objectives. By reducing agency problems, promoting transparency, and ensuring the alignment of financial goals, financial management enhances financial stability and performance for both principals and agents.

The findings of this study indicate that the use of digital accounting tools does not have a significant positive effect on the financial performance of SMEs. This result is surprising, as digital accounting is often considered a key tool in improving financial management by offering greater accuracy, efficiency, and real-time tracking of financial transactions. However, despite these potential advantages, the study suggests that the actual impact of digital accounting on financial performance may be limited or even negative for some SMEs. This can be attributed to several factors. One possible explanation for this finding is that many SMEs, particularly in developing regions, may lack the necessary resources, expertise, or infrastructure to effectively implement and utilize digital accounting tools. As pointed out by Užík et al. (2022), the adoption of digital accounting requires significant investments in training, technology infrastructure, and technical support. Without proper training and understanding, business owners and managers may struggle to fully leverage digital tools, leading to inefficiencies or errors in financial management. Moreover, the initial costs and the complexity of transitioning from manual to digital systems may outweigh the short-term benefits, causing SMEs to experience challenges rather than improvements in their financial performance. In addition, Al-Mamary et al. (2020) found that many SMEs face difficulties in adapting to digital accounting systems due to a lack of technical skills among staff and resistance to change from traditional methods of accounting. Without sufficient technical competence, digital accounting tools may not be used to their full potential, leading to suboptimal financial management practices. This highlights the need for better training and a gradual transition to digital systems for SMEs to realize the full benefits of digital accounting. Similarly, Hamzah et al. (2023b) noted that the integration of digital accounting into business operations is often hindered by a lack of understanding of how to use these tools effectively. Business owners may not fully appreciate the capabilities of digital accounting software, leading to underutilization of its features. Furthermore, inadequate implementation of digital tools can result in unreliable data or incorrect

financial reporting, which could negatively affect the financial performance of SMEs. In line with these findings, Bingley & Burgess (2024) also reported that the implementation of digital accounting tools in SMEs does not always lead to immediate improvements in financial performance. The research suggested that for digital accounting to have a positive impact, it requires the right organizational culture, sufficient technical knowledge, and proper integration with other business processes. Without these elements in place, digital accounting tools may not provide the intended benefits, and in some cases, may even complicate financial management.

5. Conclusion, Implications, and Limitations

This study concludes that factors such as financial record-keeping, financial literacy, and financial management have a significant positive impact on the financial performance of SMEs in Indonesia. Proper financial record-keeping allows SMEs to manage their financial resources more efficiently, while higher financial literacy helps business owners make better financial decisions. Additionally, effective financial management contributes to improved financial stability and growth. On the other hand, mental accounting practices, which often lead to irrational financial management, and the use of digital accounting tools that are not yet fully optimized, have a negative impact on financial performance. Therefore, SME owners need to reduce reliance on mental accounting and improve their understanding and implementation of digital accounting to support better financial performance.

The findings of this study highlight the strategic importance of improving financial management capacity among SMEs, particularly in Kuningan. The evidence that business age influences compliance with SAK ETAP underscores the need to focus on building a solid foundation of financial management for newer SMEs. Enhancing financial literacy is a fundamental step in this regard. Adequate financial literacy equips SME owners with the ability to understand the importance of accurate financial record-keeping and the implementation of accounting standards. Without sufficient literacy, SMEs risk non-compliance, which can limit their access to formal financing and growth opportunities. Therefore, community-based training programs, supported by local governments and business associations, should prioritize new SMEs, which are more vulnerable to mismanagement of their financial systems. Moreover, the digitalization of accounting systems presents a valuable opportunity to improve the efficiency and accuracy of financial record-keeping. However, without adequate technical skills, the adoption of digital tools can pose significant risks, such as data errors or over-reliance on third parties. It is thus essential for the government and related organizations to ensure the provision of inclusive technology training, alongside the development of infrastructure such as reliable internet in rural areas. With this support, digital technology can be optimized to facilitate financial reporting, increase transparency, and provide real-time access to financial data for decision-making. Additionally, sustainable financial management must remain a primary focus, especially for more mature SMEs. While these businesses may have gained experience, many fail to leverage financial data to plan long-term strategies, such as diversifying income streams or managing risks effectively. Therefore, advanced training programs on strategic financial planning are

crucial to ensuring business continuity. Collaboration between governments, business associations, and educational institutions can strengthen these efforts. For instance, local universities can play a key role by offering consultancy or training for SMEs, while governments provide incentives to encourage participation in capacity-building initiatives. With this holistic approach, SMEs in Kuningan can not only enhance their compliance with accounting standards but also strengthen their competitiveness in both local and global markets.

This study has several limitations that should be considered. The primary focus on SMEs in the fashion and retail sectors in Kuningan Regency limits the generalizability of the findings to other sectors or regions. The dynamics of financial reporting and compliance with SAK ETAP in these sectors may differ significantly from those in manufacturing, agriculture, or services, which have distinct operational complexities and financial structures. Future research should include SMEs from various sectors to provide a more comprehensive understanding of compliance behavior across industries. Additionally, this study mainly explores business age as a moderating variable without considering other factors, such as the owner's educational background, technology adoption, or access to financial training, which could also significantly influence SME compliance. Another limitation is the use of self-reported data, which may introduce bias, such as the tendency to overestimate or underestimate compliance levels. Future studies could use a mixed-methods approach to enhance data validity, combining quantitative surveys with qualitative interviews. Moreover, this study does not take into account external factors, such as regulatory enforcement, market competition, or government support programs, which may also affect SME compliance behavior. Addressing these limitations in future research would provide a more comprehensive understanding and support the development of more effective policies for SME sustainability.

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