

## Enhancing Micro, Small, And Medium-Sized Businesses Efficiency with Financial Literacy

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### Abstract

*Micro, small, and medium-sized businesses (MSMEs) play a big part in the economy, particularly in village economies. This is a result of the majority of rural firms still falling into the MSME category. Up until now, financial reports from MSMEs in rural areas have been infrequent. This is a result of MSME actors' ignorance regarding the preparation of financial reports. Low financial understanding translates into a low ability to produce financial reports. The MSME participants in Cilacap Regency's Sikanco Village, Nusawungu District, have not yet completed their financial reports for their companies. This is a result of their inexperience with financial report writing. Thus, it is impossible to accurately gauge the financial performance of MSMEs. As a result, help is required with both creating financial reports and raising awareness of financial literacy. This program helps with financial report preparation and raises awareness of financial literacy through the use of the Participatory Action Research (PAR) approach. MSME players came to the realization that financial report preparation is crucial to their firm after receiving support with it. Owners of MSME businesses become conscious of both their personal and company assets. As a result, helping to prepare MSME financial reports is crucial and beneficial for MSME participants. They make an effort to keep track of transactions and financial reports for their company, and the financial reports that have been generated are easily understandable. Residents developed an interest in and an understanding of the significance of financial reporting in order to mitigate the risk of business losses following their education. Additionally, MSME partners are growing increasingly interested in effectively managing family finances in order to improve their welfare since, through keeping track of household spending, they can identify areas where they can save more money and invest the proceeds.*

**Keywords** Financial Reports, Financial Literacy, Participatory Action Research

### INTRODUCTION

Micro, small, and medium-sized businesses (MSMEs) play a big part in the economy, particularly in village economies. This is a result of the majority of rural firms still falling into the MSME category. Up until now, financial reports from MSMEs in rural areas have been infrequent. This is a result of MSME actors' ignorance regarding the preparation of financial reports. Low financial understanding translates into a low ability to produce financial reports. This is consistent with the view that business owners' low degree of financial literacy affects their capacity to manage their finances (Anggraeni, 2015). It is possible for people to be ignorant of finance in both rich and developing nations, including Indonesia. Given that financial literacy improves financial inclusion and behavior, this condition is a severe issue (Yushita, 2017).

Low financial knowledge can be overcome by providing training to business actors. This is in line with the notion that education influences character and financial knowledge (Cossa et al., 2022). Research also indicates that the financial literacy of managers increases with financial training, which is also related to managers' confidence levels (Bayrakdaroglu & San, 2014).



Additional education provided to business actors can improve their ability to create financial reports, which are crucial for assessing business performance. This aligns with the view that financial literacy is one of the ten intelligences that humans should possess (Akmal & Saputra, 2016). Furthermore, there is research indicating that financial literacy affects the performance and innovation creativity of micro, small, and medium enterprises (MSMEs) (Fitria et al., 2021; Mang'ana et al., 2023; Sari et al., 2022; Wayhyono & Hutahayan, 2021).

Many MSME actors still do not create financial reports due to a lack of financial literacy among the owners. Therefore, it is crucial to conduct training to enhance the financial literacy of MSME owners so that performance can be improved. The aim of this community service is to enhance the ability of MSME actors to create financial reports as an effort to improve performance based on financial literacy.

## LITERATURE REVIEW

### Theoretical of Financial Literacy

Finance is one of the crucial aspects needed by society. Certainly, in managing finances, people need good knowledge and understanding of finance itself. People need to understand financial concepts and risks, as well as have sufficient financial literacy to manage their finances properly, effectively, and efficiently. Moreover, the rapidly evolving technology today also contributes to the ease of access to financial services, such as payments, money transfers, and other financial transactions, which can easily be accessed and reached by people due to the convenience of technological advancements. However, in reality, all these conveniences in accessing financial services are not accompanied by a good understanding of financial concepts and financial literacy by society.

Financial reports are information that describes the financial condition of a company, where this information can be used as an overview of a company's financial performance (Hidayati, 2018). Financial attitudes indirectly and positively influence the tendency to take risks through financial behavior (Molina-garcía et al., 2023).

Financial literacy is a series of processes or activities to improve the knowledge, beliefs, and skills of consumers and the general public so that they can manage finances better (Otoritas Jasa Keuangan, 2013). Financial literacy has a positive and significant impact on financial inclusion (Akande et al., 2023). The ability to understand financial products commonly used by the public is a reflection of everyone's financial literacy (Mihalcova et al., 2014). Financial knowledge, financial abilities, financial behavior, financial attitudes, and financial performance influence financial literacy (Hafifah, 2019).

The categories of financial literacy are 1) < 60%, which means individuals have low financial knowledge 2) 60%–79%, which means individuals have moderate financial knowledge 3) > 80%, which indicates that individuals have high financial knowledge (Chen & Volpe, 1998). MSMEs have a higher level of financial literacy than other manufacturing businesses (Asnshika et al., 2021). MSMEs are regulated in Chapter I Article 1 of Law No. 20 of 2008 (Undang-Undang No 2 Tentang Usaha Mikro, Kecil, Dan Menengah, 2008).

## Community Empowerment

Community empowerment is a concept of improving the welfare of the community in development. Development and the empowerment process are inseparable because to achieve a development goal, the process that needs to be undertaken is to empower the community so that community empowerment in development is realized. Empowerment is the concept most often used in activities to improve the capabilities of the community, emphasizing the self-reliance of the community. Community empowerment is an effort to improve the dignity and honor of the community, which in the current condition is unable to break free from the trap of poverty and underdevelopment.

The empowerment intended is to provide opportunities for the less fortunate layers of society to improve the dignity and self-esteem of the community independently. Empowerment is to empower the less fortunate communities so that they can meet their own needs. Community empowerment involves not only empowering individuals but also strengthening existing social institutions, as it aims to uplift the dignity and honor of the grassroots community that, despite its limitations, has been unable to escape poverty, ignorance, and underdevelopment. In order to empower a community, it is necessary to include individuals or groups in meeting both individual and collective needs. This process is known as empowerment. The idea that empowerment stresses the process as well as the outcomes (results) of that process lends further credence to this.

## Objectives of Community Empowerment

According to Mardikanto, the objectives of community empowerment are (Maryani & Nainggolan, 2019):

1. Institutional Improvement

By improving activities, it is hoped that institutions can be improved. Good institutions will encourage community participation in activities.

2. Business Improvement

Improvement in institutions is expected to improve the businesses conducted, thus benefiting the members of the institution and the surrounding community.

3. Income Improvement

Business improvements are expected to improve the income of all members of the institution, including the community.

4. Environment Improvement

Income improvement is expected to improve the physical and social environment because environmental damage is often caused by poverty or limited income.

5. Living Improvement

Good income and environment will improve the community's standard of living. This can be seen in health, education, and purchasing power levels.

6. Community Improvement

If every family has a good life, it will create a better community life as well.



## MSMEs

In Chapter I Article 1 of Law No. 20 of 2008 concerning Micro, Small, and Medium Enterprises (MSMEs), Micro, Small, and Medium Enterprises are defined as follows (Undang-Undang No 2 Tentang Usaha Mikro, Kecil, Dan Menengah, 2008):

Micro Enterprise is a productive business owned by an individual or a sole proprietorship that meets the criteria of a Micro Enterprise as regulated in this Law. Small Enterprise is a productive economic activity that stands alone, conducted by an individual or a business entity that is not a subsidiary or a branch of a company owned, controlled, or a part of either directly or indirectly from a Medium Enterprise or Large Enterprise that meets the criteria of a Small Enterprise as stipulated in this Law.

Medium Enterprise is a productive economic activity that stands alone, conducted by an individual or a business entity that is not a subsidiary or a branch of a company owned, controlled, or a part of either directly or indirectly from a Small Enterprise or Large Enterprise with a net worth or annual sales as stipulated in this Law.

Based on the above definitions, in essence, Micro, Small, and Medium Enterprises are a form of productive economic activity conducted by an individual or a sole proprietorship that meets the criteria of Micro, Small, and Medium Enterprises.

## Relevant Previous Studies

- 1) The study by Bayrakdaroglu and San concluded that managers with higher financial literacy levels show greater participation in the financial market by reducing information constraints. Another behavioral factor that influences market participation is extremely low self-confidence among managers participating in this study. This may be due to limited market participation among small business managers. Financial training is also related to managers' confidence levels (Bayrakdaroglu & San, 2014). This research indicates that financial literacy is crucial in business management, so the practitioners will provide additional financial literacy to MSME owners.
- 2) Another study concluded that MSME owners need to develop good financial attitudes in managing their businesses to achieve optimal business performance (Fitria et al., 2021). This community service is a development of that research, where the practitioners will provide mentoring in MSME financial management to achieve better business performance.
- 3) The research by Wahyono and Hutahayan confirms the influence of financial literacy on the performance and creative innovation of MSMEs in Central Java. This implies that with good financial literacy, MSMEs are expected to make the right financial management and decisions to improve performance and innovation. With these findings, significant support is expected from the government as a regulator, academia as an educator, the private sector as a catalyst, and the community as a driver of financial literacy development for MSMEs in Central Java. The lack of studies in the literature underlines the potential contribution of this further study (Wayhyono & Hutahayan, 2021). This research shows that financial literacy affects the performance of MSMEs,

so the practitioners will provide mentoring to improve the financial literacy of MSMEs for better performance.

- 4) The study by Anshika et al. found evidence that entrepreneurs with higher levels of education have higher levels of all types of financial literacy. The gross profit ratio of the business is the most important factor influencing the degree of financial literacy among entrepreneurs. The degree of the entrepreneurs' three forms of financial literacy increases with the company's gross profit ratio. From a policy standpoint, this research suggests that businesses should donate a portion of their earnings to training staff members in financial literacy. The government ought to assist MSMEs in educating businesses so they can become more financially literate (Anshika et al., 2021). This research highlights the importance of providing financial education to employees, so the practitioners will provide mentoring in financial education to MSME owners or their employees.

## METHOD

The methodology of this community service is conducted using the Participatory Action Research (PAR) method, which is a systematic investigative approach that allows practitioners to find effective solutions to everyday problems (Stringer, 2013). Participatory Action Research (PAR) is one model that involves all relevant parties in examining an ongoing action to bring about change and improvement towards a better direction. The underlying reason for conducting Participatory Action Research (PAR) is to achieve the desired change outcomes. This type of PAR has three criteria: participation, research, and action. All three criteria are interrelated and must be implemented in action. These three criteria synergize to change or improve from the previous state (Afandi, 2015).

The roles of practitioners in Participatory Action Research (PAR) include being planners, leaders, designers, facilitators, educators, listeners, observers, catalysts, and final coordinators. In carrying out Participatory Action Research (PAR) activities, there are six steps, including learning in action, where researchers and the community discuss planning, investigation, evaluation, training, and mapping. The second step is exploring problems, where researchers create a design that includes scheduling, community responses, and mapping sources. The third step is fact-finding and listening, where researchers learn from facts, findings, and listen to community information and voices. The identification of all pertinent stakeholders, including sociological analysis, community assets, and interests, is done in the fourth step, "Knowing the Actors." When evaluating choices, which is the fifth phase, researchers get recommendations from pertinent parties. The sixth phase involves comprehending the system as a whole, which requires researchers to perform domain analysis on domains like ecology, activities, challenges, choices, and social domains (Saliyo, 2019).

This community service activity will be carried out by participants in groups and individual mentoring. The benefits of grouping participants include having more information compared to individuals, and group members are more likely to gain a good understanding



of themselves (Burke, 2011). After being conducted in groups, practitioners will also individually guide MSME actors in creating financial reports.

## RESULTS AND DISCUSSION

This community service aims to assess the extent of understanding in MSMEs, especially in Sikanco Village, regarding financial report preparation. In the current business growth and development, MSMEs face increasingly fierce competition. The rapid economic development and the abundance of competition require sound short-term and long-term decision-making. Every business will always generate income over time. Therefore, an MSME must record financial transactions to track the costs incurred and revenues generated within the business. Financial transaction recording should not be done haphazardly, as proper recording can significantly affect the success of the business. The process of recording financial transactions is often referred to as bookkeeping. Bookkeeping is the systematic and orderly recording of all financial transactions conducted by a company. A healthy MSME can be determined by its financial statements or financial reports. Besides financial reports, a business must also maintain financial records as a report of transactions that have occurred. Financial reports and records serve as benchmarks for the success of an MSME.

The objective of this activity is to provide understanding and knowledge to the MSMEs in Sikanco Village about simple financial report preparation. This is done through preparation, implementation, and evaluation stages. The first stage is preparation, which involves direct surveys to assess the conditions in the field or MSME centers, determining which MSMEs are willing to be assisted in financial report preparation. The second stage is implementation, where education is provided first, followed by a question-and-answer session to ensure understanding of how MSME financial reports are prepared and the importance of financial reporting for MSMEs. Subsequently, the MSMEs try to make financial records on a daily basis. The evaluation stage assesses the results achieved by visiting the business premises to determine the depth of understanding of small business owners regarding financial reports.

Financial recording is used for reporting transactions that occur on a daily, weekly, and monthly basis. The results of these records become a financial report for the business. This report is used as a reference to assess the current business conditions. Financial transaction recording is the process where a company records in detail all financial transactions that affect changes in assets, liabilities, capital, income, and expenses. This financial recording process must be supported by evidence that will be used as accountability for the transactions that have been conducted. Since financial transactions consist of two types, internal and external financial transactions, evidence of financial transactions also consists of two types, internal and external evidence of the company's transactions. This community service activity is conducted in Sikanco Village, Nusawungu, Cilacap, specifically at UMKM Bunga Abadi, Tahu Crisp Mas Jo, and Risol Ibu Susi. The aim is to provide training to enhance insight and knowledge regarding the importance of financial report preparation for MSMEs and the process of financial report preparation. The activity

gathers data through interviews, socialization, and direct assistance to the owners of these three MSMEs. There are two activities in this community service: providing training on the importance of financial report preparation for MSMEs and assisting in the preparation of simple financial reports according to the Indonesian Financial Accounting Standards for Micro and Small Entities (SAK EMKM), which are manually prepared. The goal is to help provide understanding and enable MSMEs to record their finances so that they can assess the financial position of their business.

In the preparation of simple financial statements, several solutions can be implemented to address issues in MSMEs in Sikanco Village as follows:

**Recording Phase:** Business owners conduct transactions, then record the transaction evidence in a journal. Afterward, they transfer the book (post) with the account names used from the general journal to the general ledger.

**Summarizing Phase:** The trial balance, adjustments, and working papers are part of the summarizing phase. Temporary balances in the general ledger serve as the basis for trial balance data. Adjustments use data on supplies used and equipment depreciation. After the trial balance is prepared and adjusted, a working paper is created to facilitate obtaining adjusted trial balance data for financial statement preparation. The working paper includes Trial Balance, Adjustments, Adjusted Trial Balance, Income Statement, Statement of Changes in Equity, and Balance Sheet.

**Reporting Phase:** The reporting phase involves the preparation of financial statements. The financial statements that must be prepared by MSMEs include the Balance Sheet, Income Statement, Statement of Changes in Equity, and Cash Flow Statement. The Balance Sheet presents information about assets, liabilities, and equity at the end of the reporting period. Items covered in the balance sheet include cash and cash equivalents, inventory, fixed assets, and equity. The Income Statement provides information about income and expenses during the reporting period. Items covered in the income statement include revenue and financial expenses.

After completing the financial statements, a closing entry is made and then posted to the general ledger. Subsequently, a post-closing trial balance is prepared, which becomes the opening balance for the next period.

Many business owners still feel that preparing financial statements according to financial accounting standards is unnecessary. This is due to a lack of information and awareness among business owners regarding the importance of preparing financial statements in accordance with accounting standards. The difference in perspectives is the cause, as business owners believe that preparing simple statements will only make things difficult. However, the preparation of financial statements in accordance with standards is actually a way to facilitate companies in analyzing and making strategic decisions. Errors in preparing financial statements can result in incorrect decision-making, with accounts being reported incorrectly in subsequent periods.

After conducting community service on assisting in the preparation of financial statements for MSMEs, it can be concluded that one of the reasons MSMEs do not prepare financial statements is due to a lack of knowledge and training on the importance of financial



statement preparation to understand their business's financial position. MSMEs feel that financial statement preparation is not important for their business. After receiving assistance in preparing financial statements, MSMEs realize that preparing financial statements is crucial for their business. Business owners then understand their personal assets and their business's assets. Therefore, assisting in the preparation of financial statements for MSMEs is crucial and beneficial for MSME owners. The financial statements that have been prepared can be well understood, and they strive to continue recording transactions and financial statements for their business. Hence, it is hoped that MSME owners will continue to record financial statements for the benefit of their business.

The Financial Literacy Focus Group Discussion (FGD) was held on Saturday, September 16, 2023. This FGD provided knowledge and taught how to manage and record finances for MSME actors, as well as for family finances for MSME partners. The aim was for MSME actors to be familiar with applying financial reporting in their businesses, and for MSME partners to manage family finances effectively. The event took place in Sikanco Village, Nusawungu District, Cilacap Regency, and was attended by 42 people, consisting of MSME owners and their partners, who are residents producing MSME products from their homes and then delivering the results to MSME owners.

The residents of Sikanco Village were very enthusiastic about participating in the FGD because they gained new insights into managing finances well. The topics covered for the residents of Sikanco Village included financial literacy, family finances, and MSME finances. Educating the community to improve understanding of finance is crucial. With rapid development and economic growth, financial institutions play an important role in society.

Financial literacy is essential as a basic need for everyone to avoid financial problems. Lack of knowledge about financial literacy can lead to losses for individuals, resulting in extravagant spending, lack of prudence in managing credit cards, difficulty in investing, or accessing financial markets. Thus, good financial literacy can improve living standards, minimize wrong decisions regarding economic and financial issues, and encompass the ability to differentiate financial choices, discuss money and financial matters without discomfort, plan for the future, and respond competently to life events affecting daily financial decisions, including general economic events. Finance is one of the important aspects needed by society. Managing finances requires good knowledge and understanding of finance itself. Society needs to have an understanding of financial concepts and risks, as well as sufficient financial literacy to manage their finances correctly, effectively, and efficiently. Furthermore, the rapid development of technology has made it easier for people to access financial services, such as payments, money transfers, and other financial transactions, due to the ease of technological advancement. However, in reality, despite all the ease of financial access, it is not accompanied by a good understanding of financial concepts and financial literacy by the public.

Family finances, fundamentally, must also be managed and sustained with financial literacy. Families with good financial management will achieve good fulfillment of family living needs. Managing finances not only involves managing income and expenses to meet



basic human needs, but also planning which funds will meet needs when entering a non-productive age for the future. Financial management in families is a way to manage family finances systematically and carefully through planning, implementation, and evaluation stages. The amount of income in a family is indeed one of the factors in meeting family needs, but the most important thing is the skill in managing family finances. Without knowledge of financial management (family financial planning, implementation, and evaluation), the family's life can be expected to experience problems that ultimately disrupt the peace and prosperity of the family. Family life is very complex, so it is very important to regulate and plan finances within the family, where we can find a practical performance in the development of transparent and accountable accounting in managing family finances for daily needs.

Finance in MSMEs is crucial to manage in order to understand the profits and losses of the company. Financial management is one of the important aspects for the progress of a company. Financial management can be done through accounting. Accounting is a systematic process to generate financial information that can be used for decision-making by users. As long as MSMEs still use money as their exchange tool, accounting is very much needed by MSMEs. Accounting will provide several benefits for MSME actors, including:

- a) MSMEs can understand the financial performance of the company.
- b) MSMEs can identify, sort, and differentiate between company assets and owner's assets.
- c) MSMEs can understand the position of funds, both sources and uses.
- d) MSMEs can create accurate budgets.
- e) MSMEs can calculate taxes.
- f) MSMEs can track cash flow over a specific period.

Considering the benefits of accounting, MSME actors should be aware that accounting is important for their company. The use of accounting can support the progress of MSMEs, especially in financial matters. Increased profits can also be planned using accounting. With increasing profit levels, the development of MSMEs will be better, making them a real solution to economic problems in Indonesia. However, many MSMEs have not yet used accounting to support their business activities. Reasons why MSME actors do not use accounting include considering accounting to be difficult and unimportant.

MSME actors find it difficult to use accounting in their business activities. This is because there are no guidelines or books that can be used as references to learn how to manage MSME finances. The books currently available do not focus on managing MSME finances. There are several titles of accounting books for MSMEs, but their contents are similar to those for large companies. Many transactions that occur in MSMEs, such as bartering or service exchanges, are not provided as examples in books, so when these transactions occur, MSME actors prefer not to record them. If there are many similar transactions that are not recorded, it will certainly have a negative impact on the financial performance of the company. Apart from the lack of specific books discussing transactions in MSMEs, many MSME actors are reluctant to read books.

Although creating financial reports may seem difficult for MSME actors or residents of Sikanco Village because they are not used to recording the inflow and outflow of money,



the MSME actors in Sikanco Village have a high spirit to learn and practice creating financial reports for their businesses. Because after being educated, residents become interested and understand how important it is to create financial reports to avoid business losses. And MSME partners become more interested in managing family finances well so that their welfare can improve because by recording household expenses, they realize which expense items can be further saved, and the savings can be invested.

## CLOSING

### Conclusion

Many MSMEs in Sikanco Village are not aware of and have not made financial reports for their businesses. This is due to several factors: limited capital, lack of knowledge about financial reporting, and the old age of MSME actors. After the financial report creation assistance, MSME actors realized that financial reporting plays an important role in their businesses. MSME owners now understand their personal assets and business assets. Thus, the assistance in creating financial reports for MSMEs is very important and helpful for MSME actors. The financial reports that have been created can be understood well, and they strive to continue recording transactions and financial reports for their businesses. After being educated, residents become interested and understand how important it is to create financial reports to avoid business losses. And MSME partners become more interested in managing family finances well so that their welfare can improve because by recording household expenses, they realize which expense items can be further saved, and the savings can be invested.

### Recommendations

For the Sikanco village government, it is advisable to further educate MSME owners about the importance of preparing financial reports so that they are more enthusiastic about recording their business bookkeeping. Because by keeping records, MSMEs can determine the net profit of their business, making it easier to develop their business. In addition to MSMEs, the Sikanco village government should also educate all residents to record household income and expenses. By doing this, household finances will be more organized, and residents can identify expenses that can be further reduced, which can then be used for savings and investment. This way, the welfare of the Sikanco village community will improve.

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