
**FINANCIAL LITERACY, DIGITAL TRANSFORMATION ADOPTION, AND
THEIR SIGNIFICANCE TO THE MSMEs PERFORMANCE
IN BANDUNG CITY**

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Abstract: Financial and digital literacy has been recognized as a crucial information resource for financial decision-making, but the impact of MSME's financial and digital literacy on sustainability has received little attention. This study intends to examine the growth of MSME's financial knowledge and technology adoption-related obstacles. A solid business foundation, which is sorely needed, can be created by training MSMEs about financial and digital literacy in a systematic, integrated, and sustainable way. This study is quantitative research considering it employs descriptive statistical analysis of numerical data, especially the partial least square method, to examine the impact of financial and digital literacy on the performance of MSMEs. The 237 respondents in Bandung who participated in a self-administered survey were used to get the data during the third quarter of 2022. The study proved that the performance of entrepreneurs was statistically influenced by financial literacy and digital transformation adoption. Comparing the two major attributes, digital transformation has a higher score in impacting the MSME's performance. Bandung is one of the key pillars of the local economy, especially MSMEs where performance is affected majorly by digital transformation adoption.

Keywords: Financial Literacy, Digital Transformation, MSME's Performance, Bandung City

Abstrak: Literasi keuangan dan digital telah diakui sebagai sumber informasi penting untuk pengambilan keputusan keuangan, tetapi dampak literasi keuangan dan digital UMKM terhadap keberlanjutan kurang mendapat perhatian. Penelitian ini bermaksud untuk mengkaji pertumbuhan pengetahuan keuangan UMKM dan hambatan terkait adopsi teknologi. Fondasi bisnis yang kokoh, yang sangat dibutuhkan, dapat diciptakan dengan melatih UMKM tentang literasi keuangan dan digital secara sistematis, terintegrasi, dan berkelanjutan. Penelitian ini merupakan penelitian kuantitatif mengingat menggunakan analisis statistik deskriptif data numerik, khususnya metode Partial Least Square, untuk mengkaji dampak literasi keuangan dan digital terhadap kinerja UMKM. Ke-237 responden di Bandung yang mengikuti survei swakelola digunakan untuk mendapatkan data selama kuartal III-2022. Studi ini membuktikan bahwa kinerja wirausahawan secara statistik dipengaruhi oleh literasi keuangan dan adopsi transformasi digital. Membandingkan dua atribut utama, transformasi digital memiliki skor yang lebih tinggi dalam mempengaruhi kinerja UMKM. Bandung merupakan salah satu pilar utama perekonomian lokal, khususnya UMKM dimana kinerjanya sangat dipengaruhi oleh adopsi transformasi digital.

Kata Kunci: Literasi Keuangan, Transformasi Digital, Kinerja UMKM, Kota Bandung

INTRODUCTION

The role of MSMEs in industrialized countries such as the United States, Japan, Germany, and Italy provides the basis that they are one of the important foundations of economic operations. This problem is closely related to the functioning of government in a country with a large number of MSMEs. Likewise in Indonesia, MSMEs play a role as a sector that is responsible for creating job opportunities for Indonesian workers, MSMEs play an important role in the sustainability of the Indonesian economy. According to the Central Bureau of Statistics, MSMEs are business units classified into micro, small, and medium enterprises based on the quantity of labor. MSMEs added to Indonesia's Gross Domestic Product (GDP), which continued to increase from 2012 to 2016. MSMEs now consume 97.22 percent of the workforce, up from 96.99 percent previously (Alfrian & Pitaloka, 2020; Utami et al., 2021). MSMEs were able to survive the crisis well, act as a buffer, and recover quickly. Increasing access to resources is one method of developing MSMEs that will help them advance to class (Limanseto, 2022).

The ability of MSMEs to contribute to economic development has been hampered by a lack of financial services, especially from formal financial institutions. This is due to MSME owners and managers who have a level of financial literacy and optimizing the adoption of digital tools to help increase the sales and performance of MSMEs that are insufficient. As a result, financial literacy through business training leads to the development of financial knowledge and business skills, which are critical to the success of MSMEs in developing countries (Bongomin et al., 2017). The Ease of Doing Business (EODB) 2020 index places Indonesia in the fifth lowest position in ASEAN. According to a World Bank survey of 190 countries, Indonesia is ranked 73rd with a score of 69.2. Meanwhile, Singapore is ranked second with a score of 86.2, Malaysia is ranked 12th with a score of 81.5, and Thailand is ranked 21st with a score of 80.1 in other ASEAN countries (Gusman et al., 2021).

According to the results of research by Gusman et al. (2021), men and women have an average score of financial literacy that is almost the same, the results show that men have a greater opportunity to have a positive impact on MSME performance because the average financial literacy score in men is 10 points higher. On the other hand, the education and majors of the founders have no significant effect on the performance of MSMEs; what matters is their financial knowledge. MSME assets also have a positive effect on MSME performance. This influence could be because assets provide capital for MSMEs to avoid bankruptcy and learn more about their business.

Financial literacy can influence one's perspective on a company's financial situation and strategic financial decision-making, which enables business leaders to manage their finances appropriately. MSME owners must be able to handle their money well to boost their business success. The low level of financial literacy in developed and developing countries based on the results of the study concluding the importance of designing appropriate financial education and other related policy interventions to improve the ability to manage personal finances, as well as literacy for the benefit of increasing individual socioeconomic welfare and building an inclusive financial system and economic growth sustainability (Usama & Yusoff, 2019).

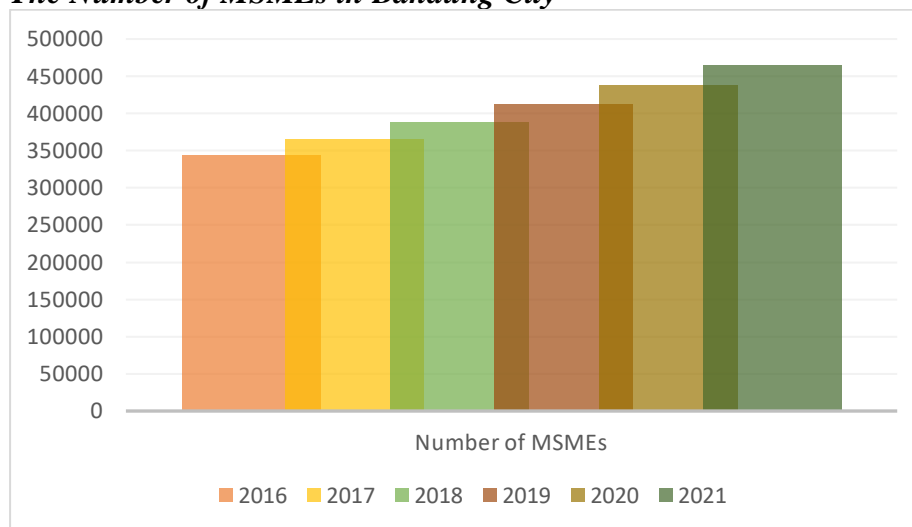
Moreover, technological progress and human resource advancement have become the two main drivers for long-term economic and social development as well as global leadership in all aspects of contemporary countries (Gusman et al., 2021). Competition in international markets has historically been the domain of large companies, while small and medium enterprises are local or regional. Good mastery of financial literacy is certainly closely related to the ability of MSME actors to access available financial systems such as banking. Indonesia is now starting to use the latest technology in conducting financial transactions. According to Bank Indonesia, cash transactions accounted for 99.4% of all retail transactions in Indonesia. In contrast, only 0.6% of non-cash traffic using electronic payment methods is covered. Indonesia remains the highest and most negative in cash transactions compared to other

ASEAN countries such as Thailand with 97.2% and Singapore with 55.5% (Rahadi, Putri, et al., 2021).

MSME performance is influenced by two factors: internal factors and external factors. Internal factors include aspects of human resources, production and operations, marketing, and finance, while external factors include aspects of government policies and related institutions that can affect MSME performance improvement (Satiti, 2020). The success of MSMEs is also influenced by the financial inclusion of MSME actors. Internal factors can affect the success of SMEs directly or indirectly. The indirect effect will be mediated by the financial inclusion variable of MSME actors which consists of the availability/access to financial services. The success of MSMEs is measured by the following indicators: Sales growth, capital growth, employment growth, market growth, and profit growth (Riwayati, 2017).

The condition of MSMEs assisted by the West Java Chamber of Commerce during the Covid-19 pandemic caused conditions to not be able to choose, they must have human resource capabilities in the form of training programs, despite the rising number of MSMEs as seen in Figure 1 below. The competence in the preparation of financial reports is still very low, but it is very much needed by MSMEs assisted by the West Java Kadin generation 4.0 at this time to be successful in entrepreneurship, so training in the preparation of financial reports is needed. Human Resources training regarding finance is still constrained by the lack of awareness of MSMEs assisted by the West Java Chamber of Commerce, even though financial accounting HR training programs, in general, can open access to banking financing (Hendiarto et al., 2021).

Figure 1
The Number of MSMEs in Bandung City



Source: Dinas Koperasi dan Usaha Kecil Jawa Barat (2021)

Based on research conducted by Dai et al. (2020), several variables have been tested to influence the performance of MSMEs such as capital, behavior, change, and financial behavior. MSME actors already have a habit of saving to maintain the continuity of their business in the future, based on several reasons: First, the name of the business goes up and down so that when it goes down, they already have savings. The second is for urgent necessity. Third, preparation for old age. Fourth, prepare to start a business or develop a business and send children to school. Meanwhile, some MSMEs still incorporate their business financial assets with private property. Thus, it is necessary to study deeply about financial literacy and the use of non-cash transactions by MSMEs in Bandung City to determine the effect on MSME performance, then a model can then be made to improve MSME performance in Bandung City so that it can become a standardized business unit to increase productivity and performance. In 2022,

research will be conducted based on the concept of financial literacy and the adoption of digital transformation to determine the effect on MSME performance.

LITERATURE REVIEW

Financial Literacy in MSMEs

Financial literacy is defined as information, beliefs, and skills that impact attitudes and behaviors to improve decision-making and financial management to achieve prosperity (Dai et al., 2021; Satiti, 2020). According to Utami et al. (2021), Firli (2017), and Dai et al. (2021), looked at five variables to assess the financial literacy of MSME owners: (1) Financial planning, budgeting, and control; (2) Bookkeeping; (3) Funding sources; (4) Respondents' knowledge of the company; (5) Risk management; (6) Economy; and (7) Investment. According to the research of Ye and Kulathunga (2019) in Sri Lanka, financial literacy has also emerged as a predictor of access to financial and financial risk attitudes. In addition, access to finance and financial risk attitudes were found to be partial mediators of the relationship between financial literacy and the sustainability of MSMEs.

Financial literacy is the ability to make decisions as a person, as an individual, or as a corporation by understanding the fundamentals of money. In the meanwhile, says that financial literacy is the understanding of financial ideas, talents, and skills connected to financial concepts, capabilities in business management, and the capacity to make generally accurate and quick business judgments in some circumstances (Buchdadi et al., 2020). Measuring financial literacy combines conceptual and operational aspects, such as awareness, knowledge, and the ability of individuals or communities to access financial institutions to carry out budgeting activities, manage savings, take loans, or make investments, depending on one's level of financial understanding (Bongomin et al., 2017; Ismanto et al., 2019).

Financial literacy is necessary for MSMEs to examine their financial affairs and make financial decisions. Entrepreneurs with financial literacy are better able to handle risk by using measures such as maintaining cash reserves, diversifying their investment portfolios, and buying insurance (Ye & Kulathunga, 2019). Financially literate people will be able to set financial objectives, create financial plans, manage their money, and make wise choices while utilizing financial goods and services (Buchdadi et al., 2020). Behavioral finance is based on several presumptions and ideas about how people behave economically as well as their emotional reactions, personality traits, and likes. This is because interactions between social and intellectual beings are what ultimately lead to a decision to act. Financial behavior is based on highly complicated psychological processes and includes social components (Kostini & Raharja, 2020).

Digital Transformation and Cashless Society in Business

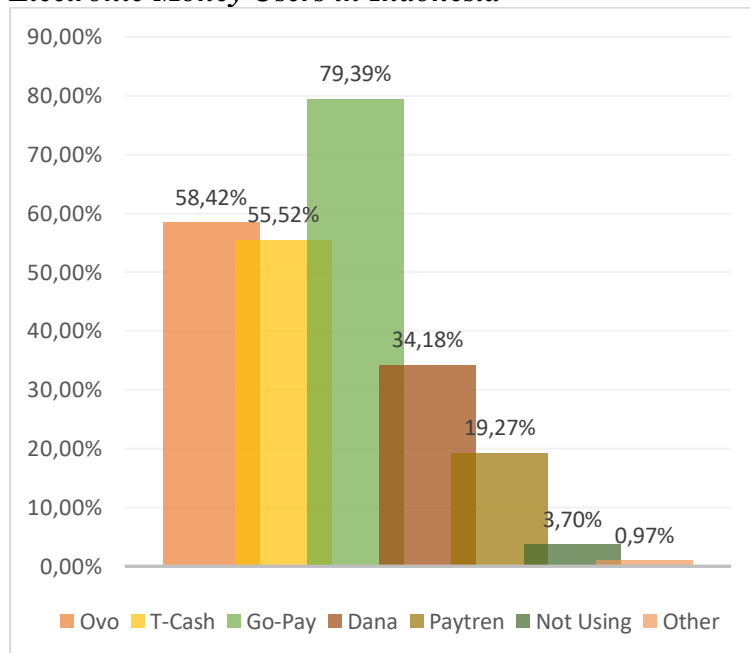
The fourth industrial revolution, marked primarily by digital transformation, is booming. The essence of digital transformation is to use the digital characteristics of copying, linking, simulation, and feedback to measure all aspects of the business (Rahadi, Candra, et al., 2021). Micro, small, and medium enterprises (MSMEs) must adapt to a new round of scientific and technological revolutions and industry transformation trends; capture the advantages of digital technology; and enhance their ability in rapid perception, agile response, and smart decision-making in the digital age to improve their ability to face risk and sustainable development (Rahadi, Dewi, et al., 2021; Rupeika-Apoga et al., 2022; Teng et al., 2022). According to research by Koe and Sakir (2020), in the face of the wave of digitalization and driving the adoption of e-commerce among entrepreneurs in Malaysia, building strong and close relationships between entrepreneurs is essential. There are many trade associations in Malaysia.

Several firms in Indonesia offer electronic wallets or electronic payments. Additionally, a sizable number of people utilize it. It is anticipated that the introduction of electronic wallets and payments would make it easier for the community to conduct financial transactions, which are already known to be quite complicated in the modern period. E-wallets may be used to pay

for all of the community's requirements, including internet and power, in addition to purchasing and selling goods and services (Wulantika & Zein, 2020).

The term "cashless payment system" refers to an economic arrangement in which products and services are exchanged through an electronic transfer mechanism rather than cash. The cashless payment system is separated into two parts: banking services (debit cards, credit cards, ATM cards, m-banking) and non-banking services (Go-pay, Ovo, ShopeePay, Dana) (Lenniawati & Anastasia, 2020; Rahman et al., 2020). Automatic electronic money that has been inputted by users can be used virtually at any time as long as the balance is sufficient (Hastomo & Aras, 2018). Based on a questionnaire conducted by Jakpat & OJK in 2018 for 825 respondents, Gopay occupies the highest user using a percentage of 79.39% as seen in (Wikannanda et al., 2019).

Figure 2
Electronic Money Users in Indonesia



Source: Wikannanda et al. (2019)

Several studies report that the six dimensions of a company's strategic vision, consistency of vision and investment in digital transformation, conformity of innovation culture, ownership of adequate intellectual property assets and knowledge, the power of digital capabilities, and the use of digital technologies can be improved. This enables businesses to achieve a successful competitive position through digital transformation (Teng et al., 2022). Digital financial services as part of financial innovation, on the one hand, can lead to faster bank growth. However, on the other hand, it can also create bank fragility, especially in times of crisis. Therefore, the quality of regulation must be considered to minimize incentives for moral hazard and excessive risk-taking behavior (Trinugroho et al., 2017).

The digital divide has three types, namely access divide, usage divide, and quality of use divide. The access divide relates to the ownership gap of access to information technology. Meanwhile, the usage divide is in the form of gaps in the differences in the use of information technology. The quality of use divide is a gap in the quality of technology used in everyday life. The gap in terms of the use of technology itself is related to the stereotype inherent in society that technology is closer to men's lives, the lack of interest, and the lack of capability to use it (Anggraini & Supriyanto, 2019).

MSME Performance

Around 88% of the MSMEs experienced a decrease in demand during the pandemic. As for medium-sized enterprises, the figure is even larger, standing at 91%. Micro and small enterprises experienced 86% and 87% lower demand, respectively. A similar pattern could be discerned when we look at the heterogeneity impact in terms of the gender of the owner. Related to the percentage decrease in demand for products, a third of all MSMEs reported a 40% to 60% decrease in demand for their products. The 40% to 60% drop is felt by 45% of medium-sized enterprises, while the same drop was experienced by 29.1% and 28.3% of micro and small enterprises, respectively. In terms of gender, more than 30% of MSMEs owned by both males and females experienced a 40% to 60% decrease in demand (UNDP Indonesia & LPEM FEB UI, 2020).

Company performance is a complete display of the state of the company for a certain period as a result of achievement that is influenced by the company's activities in utilizing its resources. Several factors affect the performance of MSMEs, including: a) internal factors, such as human resources, finance, marketing, and operational factors; and b) external factors, such as market information, social, economic, and cultural conditions in the environment around MSMEs, country-level economic policies, and the availability of raw materials from suppliers (Satiti, 2020). One of the performance measures that are easiest for MSME owners to know is their sales level which will affect the cash flow of MSMEs.

Financial activity, in which the owner of an MSME plays an important role in the decision-making process, is one of the performance characteristics of small and medium-sized enterprises. Marketing, human resources, excellent governance, and operations are non-financial factors that affect the performance of MSMEs (Gusman et al., 2021). Financial literacy training among microenterprises in Kenya has a significant positive impact on their performance. Thus, financial literacy facilitates the expansion of MSMEs and increases their profitability, productivity, and competitive advantage (Bongomin et al., 2017).

RESEARCH METHOD

This study is part of a quantitative study that allows researchers to perform hypothesis testing using measures of financial data and the performance of population samples from subjects. This survey tool uses surveys, so the data used is the key. The information collected is based on the dissemination of on-site questionnaires, interviews, and analysis at the time of the survey. This research was conducted on MSMEs in the city of Bandung which was recorded in 2021 as many as 464,346 MSMEs as their population has been divided into several industrial sectors according to the type of business. Bandung as the capital of West Java is listed as a member of the UNESCO creative city network.

Purposive sampling used in this study aims to examine the population which is the whole MSMEs in Bandung City. The study's sample size was altered to fit the analytical technique, partial least squares with structural equation modeling (PLS-SEM). To gather quantitative information, questionnaires were randomly given to the MSMEs and asked about the number of workers and annual revenue of the business. Owners, managers, and executives are the ones who responded since it is believed that they are the ones that know their firm the best. This study employed an internet form as a technique for collecting data. Based on information from regional governments, questionnaires were delivered to several MSME associations in the city of Bandung and mailed directly to MSME contacts. The distribution of the questionnaire resulted in 237 valid responses.

The measurement scale used in the questionnaire uses a level interval scale of 5, from (1) strongly disagreeing to (5) strongly agreeing. PLS-SEM was used in this study as a data analysis technique to test hypothesized models. To test the validity or validity of research results, validity, and reliability tests are needed to test the results of the questionnaire. Financial literacy is measured based on items of knowledge, benefits, economic development, business opportunities, asset management, and financial control. Insurance, financial goals, risks as well

as investments. Then for the digital transformation aspect, it is measured using non-cash transactions in transactions with customers, financial management, suppliers, and satisfaction in the use of non-cash transactions. Meanwhile, the performance of MSMEs is measured by increasing sales, capital, number of workers, marketing programs, consumer origin, profit, and financial and business management developments.

RESULTS AND DISCUSSIONS

Descriptive Analysis

The questionnaire results showed 237 MSMEs were respondents of which 57.8% were business owners involved in daily business activities, who come from various industrial sectors such as fashion, food and beverages, accommodation, tourism, and retail. As many as 51.1% of respondents were aged 21-30 years, 28.3% were aged 31-40 years and the rest were over 40 years old. Based on annual revenue in rupiah, 80.6% of SMEs have revenues < 300 million per year, 19% have revenues of 300 million-2.5 billion per year, and the remaining 0.4% have revenues > 2.5 billion per year.

Model Analysis

Measurement models are assessed to ensure adequate quality of measurement construction. Assessment in the form of factor analysis, measurement of indicator reliability, and discriminant validity. Each assessment has a minimum recommended value on the measurement results. For *outer loading* items of at least 0.7, *Cronbach's Alpha* (CA) internal consistency of at least 0.7, and *Average Variance Extracted* (AVE) of at least 0.5. The results showed that the *outer loadings* and CA indicators on each construct were higher than the minimum values. Furthermore, the AVE results for each construct exceed the minimum value indicating validity is achieved. The full result regarding the measurement construct is shown in Table 1.

Table 1

Validity and Reliability Test

Constructs and Indicators	<i>Outer Loadings</i>	<i>Cronbach's Alpha</i>	<i>AVE</i>
Financial Literacy		0.76	0.677
Financial Knowledge	0,725		
Economics Development	0,9		
Digital Transformation		0.912	0.699
Cashless Transaction	0,744		
Digital Safety	0,493		
Speedy Transaction	0,698		
Financial Management	0,809		
Preferred Payment	0,406		
Network Stability	0,29		
Business Performance		0.864	0.683
Sales Growth	0,75		
Capital Growth	0,845		
Human Resources Growth	0,739		
New Acquired Consumer	0,709		
Profit Growth	0,823		
Digital Transformation to Business Development	0,701		

Source: Researcher (2022)

Evaluate Model Measurements

After the analysis using the PLS-SEM algorithm was done, it is resulting the evaluation of the hypothesis relationship and the path coefficient between constructs are shown in Table 2. This study used several criteria to assess hypotheses, including coefficient, *t*-statistics, and *p*-values. The value of the coefficient indicates the interrelationship between variables; If the value of the coefficient is positive, then the relationship between the variables is positive. In

this study the significance level used was 5%, thus the confidence level is 95%, and the *t*-statistical value was 1.97. If the *t*-statistical value indicates a > value of 1.97 then the influence between the variables is significant. *P*-values aim to test the significance of a research result, the *p*-values that must be obtained for a hypothesis to be accepted are < 0.5% or < 0.005. If all three criteria are met, then the previously formulated hypothesis is acceptable, and vice versa; If one of the criteria does not meet, it means that the previously formulated hypothesis is not accepted.

Table 2
Model Measurement

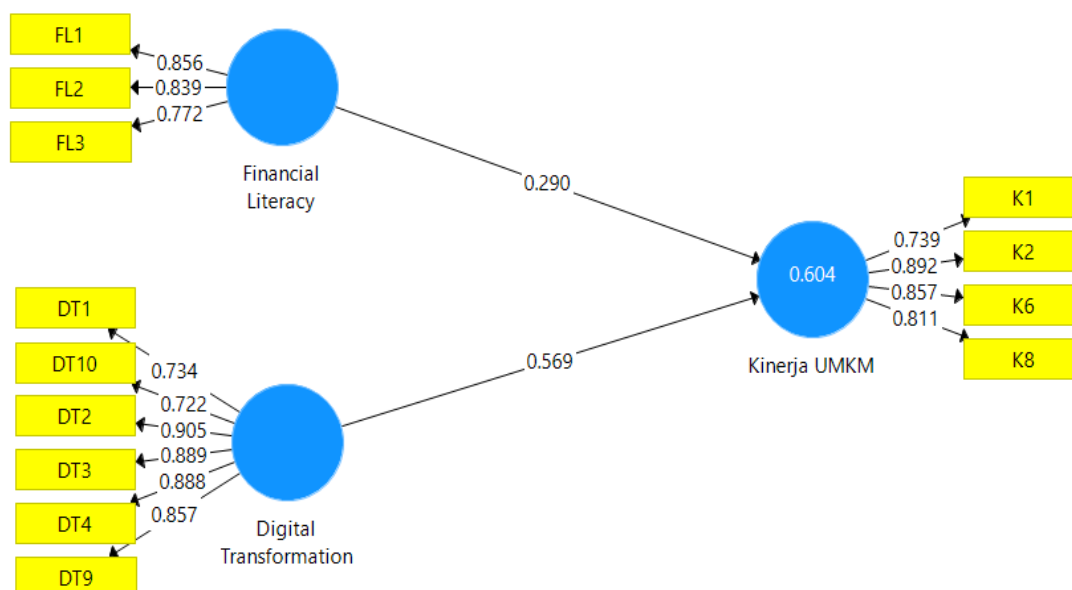
Hypothesis	Path	Coefficient	T-statistics	P-Values
H1	Financial Literacy -> MSMEs Performance	0.29	4.571	0
H2	Digital Transformation -> MSMEs Performance	0.569	9.492	0

Source: Researcher (2022)

Figure 2 shows the positive effect of two constructs on MSME performance, namely financial literacy, and digital transformation. Overall, the relationship hypothesis in H₁ and H₂ is supported by data that emphasizes financial literacy and digital transformation as significant predictors of MSME performance. Furthermore, financial literacy is a significant predictor of digital transformation in MSMEs. This result implies the importance of financial literacy and digital transformation in MSME business activities. These results are similar to several other studies where the performance of the MSMEs founders lead is influenced by their behavioral characteristics and financial literacy. Confidence, impulsivity, and financial action are some qualities that might affect how someone makes decisions in their work life (Gusman et al., 2021; Purwidiyanti & Tubastuvi, 2019; Usama & Yusoff, 2019).

To see how much an independent variable contributes to a dependent variable can use the *R*-square value. According to Hair, Jr. et al. (2014), the minimum value ranges used for *R*-square values are 0.25, 0.5, and 0.75. These values are described as weak, moderate, and substantial, respectively. Based on the PLS-SEM results in Figure 2, the *R*-square for MSME's performance is 0.604, and this indicates that financial literacy and digital transformation account for 60.4% of MSME's performance variance. These results suggest that conceptual models have sufficient predictive capacity on dependent constructs in this study.

Figure 2
Structural Model Assessment



Source: Researcher (2022)

The results show that financial literacy particularly financial knowledge, budgeting, and economic development has a higher score among all the 10 indicators in this variable affecting the MSME's performance. Meanwhile, the higher score of digital transformation is a cashless transaction, digital safety, speedy transaction, financial management, preferred payment, and network stability. The test results showed that all hypotheses in this study were accepted where the relationship between each variable was positive and significant. The findings of this study are expected to contribute to the literature to increase business performance among MSMEs.

CONCLUSIONS

This study focuses on the impact of financial literacy and digital transformation on the performance of MSMEs specifically in Bandung. The sampling technique used to analyze a population whose composition cannot be identified directly is known as purposive sampling. To accommodate the analytical method of partial least squares with structural equation modeling (PLS-SEM), the study's sample size was changed. Questionnaires were randomly sent to the MSMEs and inquired about the number of employees and yearly revenue of the company to collect quantitative data. Two constructs—financial literacy and digital transformation—show favorable effects on MSME performance on the *t*-statistics test. Overall, the evidence emphasizes financial literacy and digital transformation as major drivers of MSME success, supporting the association hypothesis in H₁ and H₂. Finally, the *R*-square for MSME's performance is 0.604, and this indicates that financial literacy and digital transformation account for 60.4% of MSME's performance variance. These findings imply that conceptual models in this study have enough predictive power for the dependent constructs. Further research can be conducted with a larger sampling number to gather a full vision of the MSME's performance.

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