

# The Effect of Islamic Financial Literacy and the Implementation of Islamic Accounting on the Financial Performance of MSMEs

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## Abstract

**Research aims:** This research aims to examine the effect of Islamic financial literacy and the implementation of Islamic accounting on the financial performance of Micro, Small, and Medium Enterprises (MSMEs). This study is motivated by the low level of Islamic financial literacy and the suboptimal implementation of Islamic accounting among MSME actors, which may affect the quality of financial management and business sustainability.

**Design/Methodology/Approach:** This research uses a quantitative approach with a survey method by distributing questionnaires to 90 MSME actors in Serang City, Banten. The research data were analyzed using Structural Equation Modeling Partial Least Squares (SEM-PLS) with SmartPLS software to examine the relationships among constructs and to assess the validity and reliability of the measurement model.

**Research findings:** The results show that Islamic financial literacy has a positive and significant effect on the financial performance of MSMEs. In addition, the implementation of Islamic accounting is also proven to have a positive effect on the financial performance of MSMEs. These findings indicate that MSME financial performance is not only influenced by capital and marketing factors, but also by the ability of business actors to understand Islamic financial principles and apply financial recording practices in accordance with sharia principles.

**Theoretical contribution/Originality:** This research provides a scientific contribution to the development of Islamic financial management studies, particularly in explaining the role of Islamic financial literacy and Islamic accounting implementation in improving MSME financial performance.

**Practitioner/Policy implication:** This research can serve as a reference for MSME actors, government institutions, and related stakeholders in strengthening Islamic financial literacy and encouraging the implementation of transparent, systematic, and sharia-compliant accounting practices.

**Research limitation/Implication:** This research is limited to MSME actors in Serang City, Banten, so the findings may not fully represent MSMEs in other regions with different social, economic, and business characteristics.

**Keywords:** Islamic Financial Literacy; Islamic Accounting; MSME Financial Performance.



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## Introduction

Micro, Small, and Medium Enterprises (MSMEs) constitute one of the strategic sectors that make a substantial contribution to national economic growth. The existence of MSMEs not only plays a role in increasing community income but also serves as a key sector in employment absorption, poverty alleviation, and the strengthening of regional economies (Arianto & Sofyan, 2022). Within the structure of the Indonesian economy, MSMEs represent the backbone of community-based economic activity, as they are able to survive

under various economic crisis conditions and demonstrate a high degree of flexibility in responding to market changes. This significant role has made MSMEs a sector whose development continues to be promoted by the government, particularly in terms of strengthening business capacity, improving access to financing, and ensuring sustainable business financial management. Despite their significant contribution to the national economy, most MSMEs continue to face various problems in managing their business finances (Yolanda & Hasanah, 2024). These problems include limited ability to prepare financial statements, weak transaction recording practices, the absence of separation between personal and business finances, and a low level of understanding of sound financial management principles (Herawati & Simbolon, 2025).

These conditions make it difficult for many MSMEs to measure their financial performance objectively and systematically. The low quality of financial management also affects the limited ability of MSMEs to obtain access to formal financing, particularly sharia-based financing, which requires transparency and accountability in financial reporting (Zulhelmi & Khairi, 2026). From the perspective of Islamic economics, business financial management is not only oriented toward profit maximization but must also take into account sharia principles such as honesty, justice, transparency, and business blessings. These principles position economic activity as part of worship, so every financial transaction must be free from the elements of *riba*, *gharar*, and *maysir*. Therefore, Islamic financial literacy is an important aspect that MSME actors must possess in order to understand financial management mechanisms that comply with sharia principles (Suharlina & Ferils, 2024). Islamic financial literacy does not only refer to the ability to understand Islamic financial products and services, but also includes an understanding of contracts, profit-sharing systems, debt and receivable management, and financial decision-making in accordance with Islamic law. Thus, Islamic financial literacy can be defined as an individual's ability to understand the concepts, principles, and practices of sharia-based finance, as well as the ability to apply them in daily economic activities (Azri et al., 2024).

MSME actors with a good level of Islamic financial literacy are expected to be able to manage business finances more effectively, efficiently, and in accordance with sharia principles. Such understanding can also assist business actors in determining appropriate sources of financing, avoiding transaction practices that contradict Islamic law, and improving the quality of business financial decision-making (Maulana et al., 2025). Accordingly, Islamic financial literacy is believed to have a close relationship with the improvement of MSME financial performance. In addition to Islamic financial literacy, the implementation of Islamic accounting is also an important factor in supporting MSME financial management. Islamic accounting is a system of financial recording and reporting based on Islamic sharia principles, such as justice, openness, accountability, and trustworthiness (*amanah*) (Arwandi et al., 2025). The implementation of Islamic accounting in MSMEs can be realized through honest and systematic transaction recording, the separation of personal and business finances, the preparation of transparent financial statements, and the avoidance of transactions containing non-halal elements. The application of Islamic accounting is not only intended to produce accurate financial statements but also to build trust, integrity, and long-term business sustainability (Wahyudi & Rosyidah, 2024).

In practice, the implementation of Islamic accounting in MSMEs still faces various obstacles. Most MSME actors continue to perceive financial recording as a complicated activity that is not particularly important for business continuity. The majority of MSME actors conduct economic activities in a simple manner without an adequate recording system (Fadhila & Ningsih, 2024). This condition makes it difficult for MSME actors to determine the actual financial condition of their businesses, including in calculating profit, cash flow, and operational cost efficiency. In addition, the low level of understanding of Islamic accounting standards has also resulted in the suboptimal implementation of sharia principles in business financial management. On the other hand, the development of the Islamic economy in Indonesia has shown relatively rapid growth, as indicated by the increasing number of Islamic financial institutions, Islamic financing products, and

government support for strengthening the national halal ecosystem. This condition provides significant opportunities for MSMEs to develop their businesses through a sharia-based economic system.

However, these opportunities have not been optimally utilized by MSME actors due to the low level of Islamic financial literacy and the limited implementation of Islamic accounting in business management (Al Adil et al., 2026). As a result, many MSMEs have not been able to improve their competitiveness and the quality of their financial management in a sustainable manner. Moreover, the financial performance of MSMEs is essentially influenced by various internal and external factors. Internal factors include managerial capability, the quality of human resources, financial management, and accounting recording systems. Meanwhile, external factors include access to financing, market conditions, business competition, and government policy support. In the context of this study, Islamic financial literacy and the implementation of Islamic accounting are viewed as internal factors that play an important role in improving the quality of business financial management (Utrojah et al., 2026). MSME actors who possess sound Islamic financial understanding and are able to consistently implement an Islamic accounting system are expected to improve business management efficiency, strengthen business decision-making, and enhance profitability and business sustainability. Although Islamic financial literacy and the implementation of Islamic accounting theoretically influence the financial performance of MSMEs, studies that integrate these two variables remain relatively limited (Martina et al., 2025).

In addition, most previous studies have focused more on the effect of financial literacy on financial management behavior or have only discussed the implementation of Islamic accounting partially (Junery & Aziz, 2018). Other studies have focused more on access to Islamic financing, Islamic financial inclusion, and halal-based business development; therefore, studies that simultaneously examine the influence of Islamic financial literacy and the implementation of Islamic accounting on MSME financial performance remain limited (Farida & Arifin, 2022; Zulfa, 2025). Meanwhile, most previous studies have emphasized the aspect of financial knowledge without integrating the implementation of Islamic accounting as a practical and operational financial management system. In fact, good Islamic financial understanding is not necessarily accompanied by the ability of MSME actors to apply financial recording and reporting practices in accordance with sharia principles (Fadila et al., 2024; Dhani et al., 2025). Therefore, the relationship between Islamic financial literacy and the implementation of Islamic accounting in improving MSME financial performance still requires more comprehensive empirical examination (Ulfah et al., 2026). Based on the foregoing discussion, this study is conducted to examine the effect of Islamic financial literacy and the implementation of Islamic accounting on MSME financial performance. This study is expected to provide a theoretical contribution to the development of Islamic accounting studies and a practical contribution for MSME actors in improving the quality of business financial management based on sharia principles.

## **Literature Review**

### **Islamic Financial Literacy**

Islamic financial literacy refers to an individual's ability to understand the concepts, principles, and management of finance based on the provisions of Islamic sharia. This form of literacy has developed in line with the increasing public demand for a financial system that is not merely oriented toward economic profit, but also takes into account the aspects of halal compliance, justice, and blessings in economic activities. From the perspective of Islamic economics, financial management must be carried out in accordance with sharia principles by avoiding the elements of *riba*, *gharar*, and *maysir*. Thus, every economic activity is expected not only to generate material benefits but also to embody moral and spiritual values. This understanding is important because a low level of Islamic financial literacy may cause individuals to be less capable of making appropriate financial decisions that are in accordance with Islamic principles. In financial behavior theory, the ability to understand financial information influences an individual's pattern of economic decision-

making. Individuals with a good level of financial literacy tend to be better able to plan, manage, and control their finances effectively than those with a low level of literacy. In the sharia context, financial literacy is not only related to knowledge of Islamic financial products and services, but also includes an understanding of contracts (*akad*), profit-sharing systems, zakat, and transaction mechanisms that comply with Islamic law. Accordingly, Islamic financial literacy can shape financial behavior that is more responsible, transparent, and oriented toward business sustainability. Various previous studies have shown that Islamic financial literacy affects the quality of financial management and business performance (Nurrohmah & Purbayati, 2020). Individuals or business actors with sound Islamic financial understanding tend to be more capable of managing financial risks, preparing business plans, and optimally utilizing Islamic financial services.

### **Implementation of Islamic Accounting**

The implementation of Islamic accounting refers to the application of a system for recording, measuring, reporting, and disclosing financial transactions based on Islamic sharia principles. Islamic accounting is not only oriented toward the presentation of financial information, but also emphasizes the values of justice, transparency, honesty, and accountability in every economic activity. From the perspective of agency theory, the relationship between the principal and the agent requires responsibility and information transparency in the management of economic resources. In a business context, the business owner may be positioned as the principal, while the business manager acts as the agent entrusted with managing financial activities properly and in accordance with sharia principles. When the implementation of Islamic accounting does not function properly, the potential for financial management irregularities, lack of reporting transparency, and errors in decision-making becomes greater. Problems in business financial management often arise due to weak recording systems and limited understanding of Islamic accounting principles. Such conditions may give rise to conflicts of interest between business objectives and individual behavior that is inconsistent with the principles of trustworthiness (*amanah*) and honesty (Birton et al., 2015). Within agency theory, this condition can be understood as an agency problem that emerges as a result of information asymmetry and weak internal control. Therefore, the implementation of Islamic accounting serves as an important instrument in creating a financial management system that is transparent, accountable, and consistent with the provisions of Islamic sharia. Various studies also affirm that the implementation of Islamic accounting influences the quality of financial statements and business performance. It can be stated that business actors who apply systematic financial recording in accordance with sharia principles tend to be more capable of managing cash flow, controlling costs, and increasing external stakeholders' trust in the business being operated.

### **MSME Financial Performance**

MSME financial performance refers to the extent to which a business is able to manage its financial resources effectively and efficiently in order to achieve its economic objectives. Financial performance is generally measured using indicators such as increased turnover, business profit, cash flow, operational cost efficiency, and the ability of the business to meet its financial obligations. From the perspective of agency theory, the relationship between the principal and the agent requires transparent and accountable financial management so that business objectives can be achieved optimally. In the context of MSMEs, the business owner, as the principal, delegates authority to the business manager, as the agent, to carry out operational activities and make financial decisions. When financial management is not properly conducted, the potential for misuse of resources and a decline in business performance becomes greater. Problems related to MSME financial performance are often influenced by weak financial management systems, limited ability to prepare financial statements, and insufficient understanding of business planning and control. These conditions may give rise to agency problems in the form of misalignment between business objectives and the financial management practices being implemented. In addition, weak

financial transparency and accountability may also hinder MSMEs from obtaining access to financing and improving business competitiveness. Therefore, sound financial management is an important factor in enhancing the sustainability and growth of MSMEs. Various studies also affirm that MSME financial performance is influenced by the ability of business actors to manage finances, prepare financial statements, and make appropriate business decisions (Ayem & Wahidah, 2021). As a result, MSME actors with good financial management systems tend to be better able to increase profitability, maintain cash flow stability, and sustain business continuity in the long term.

### **Islamic Financial Literacy and MSME Financial Performance**

Islamic financial literacy refers to an individual's ability to understand the concepts, principles, and management of finance based on the provisions of Islamic sharia. This literacy includes an understanding of contracts (*akad*), profit-sharing systems, business financial management, and the prohibition of *riba*, *gharar*, and *maysir* practices in economic activities. From the perspective of agency theory, a low level of financial understanding among agents may give rise to agency problems, as agents tend to make decisions that are ineffective and inconsistent with the objectives of the principal. In the context of MSMEs, business actors act as agents who are responsible for managing business resources in a trustworthy, transparent manner and in accordance with sharia principles. When the level of Islamic financial literacy among MSME actors is low, their ability to manage business finances, make business decisions, and utilize Islamic financial services becomes less optimal, thereby potentially reducing business financial performance (Alfarisy & Canggih, 2025). Several studies affirm that Islamic financial literacy plays an important role in improving the quality of financial management and business sustainability. MSME actors with sound Islamic financial understanding tend to be more capable of managing cash flow, controlling operational costs, and preparing business plans more effectively (Ariyati & Agustina, 2021). In addition, Islamic financial literacy can increase business actors' awareness of the importance of financial management that is honest, transparent, and consistent with sharia principles. This condition encourages MSME actors to be wiser in making economic decisions and to improve the quality of business financial performance (Purnamasari & Asharie, 2024). Therefore, business actors with a good level of Islamic financial literacy are expected to be able to enhance profitability, business stability, and the long-term sustainability of MSMEs. Based on the foregoing discussion, the following research hypothesis is formulated:

**H1: Islamic financial literacy has an effect on MSME financial performance.**

### **Implementation of Islamic Accounting and MSME Financial Performance**

The implementation of Islamic accounting refers to the application of a financial recording and reporting system based on Islamic sharia principles, such as honesty, openness, accountability, and justice (Oktaviana, 2022). From the perspective of agency theory, the application of a proper accounting system is necessary to reduce information asymmetry and minimize conflicts of interest between the principal and the agent. In the context of MSMEs, the implementation of Islamic accounting serves as an important instrument in creating transparent and responsible business financial management. When MSME actors do not apply systematic financial recording in accordance with sharia principles, the potential for financial management errors, inaccurate reporting, and inappropriate decision-making becomes greater. Various studies affirm that the implementation of Islamic accounting affects the quality of financial statements and the improvement of business performance (Putri et al., 2023). MSME actors who record transactions properly and in accordance with sharia principles tend to be more capable of controlling cash flow, evaluating business conditions, and improving operational efficiency. In addition, the application of Islamic accounting can also increase the trust of external parties, such as financial institutions and investors, in the business being operated (Restu et al., 2023). Thus, the implementation of Islamic accounting can assist MSMEs in improving the quality of financial management and supporting long-term business sustainability

(Pujiati, 2025). Based on the foregoing discussion, the following research hypothesis is formulated:

**H2: The implementation of Islamic accounting has an effect on MSME financial performance.**

### **Islamic Financial Literacy, Implementation of Islamic Accounting, and MSME Financial Performance**

Islamic financial literacy and the implementation of Islamic accounting are two important and interrelated factors in supporting the quality of business financial management. Islamic financial literacy provides a conceptual understanding of financial management based on sharia principles, while the implementation of Islamic accounting represents its practical application in business financial recording and reporting activities (Al Adil et al., 2026). From the perspective of agency theory, the combination of sound financial understanding and the application of a transparent accounting system can minimize agency problems and improve the effectiveness of business management. MSME actors who possess sound Islamic financial understanding and are able to consistently implement Islamic accounting tend to be more capable of managing their businesses efficiently, accountably, and with a strong orientation toward business sustainability (Arianti, 2025). Several studies affirm that the quality of financial management and the application of accounting systems have a positive relationship with improved business performance (Evriyenni, 2022). Therefore, the integration of Islamic financial literacy and the implementation of Islamic accounting is believed to strengthen the ability of MSMEs to improve profitability, business efficiency, and financial stability (Aulia, 2025). Based on the foregoing discussion, the following research hypothesis is formulated:

**H3: Islamic financial literacy and the implementation of Islamic accounting simultaneously affect MSME financial performance.**

### **Research Methods**

This study employs a quantitative approach using a survey method through the distribution of questionnaires to Micro, Small, and Medium Enterprise (MSME) actors as research respondents. The object of this study is focused on MSME actors categorized as small enterprises that have actively conducted business activities and independently managed their business finances. The selection of these MSMEs refers to business actors who operate in Serang Regency, Banten, and have used Islamic financial services. A total of 90 MSME actors participated as respondents in this study. They were selected using a simple random sampling technique, with the criteria that respondents must be active business actors who have operated their businesses for at least one year and have carried out business financial recording activities. The research instrument used was a structured questionnaire designed to measure three main variables, namely Islamic financial literacy, the implementation of Islamic accounting, and MSME financial performance. All questionnaire items were measured using a 1–6 interval Likert scale, where scores of 1–3 represent disagreement and scores of 4–6 represent agreement. The even-numbered scale approach was used to encourage respondents to provide a more definite attitude toward each statement (Arianto & Oktaviani, 2025).

### **Operational Definition and Variable Measurement**

The Islamic financial literacy variable is positioned as an independent variable that reflects the level of understanding of MSME actors regarding Islamic financial concepts, sharia transaction principles, business financial management, and the utilization of sharia-based financial services. The implementation of Islamic accounting is also an independent variable that reflects the application of financial recording and reporting systems in accordance with sharia principles, such as transparency, honesty, and accountability in business management.

Meanwhile, MSME financial performance is the dependent variable that describes the ability of a business to increase turnover, profit, operational cost efficiency, and business

sustainability. Each question indicator was developed based on a literature review related to Islamic financial literacy, Islamic accounting, and MSME financial performance, and was adapted to the context of business management in the MSME sector. All indicators are expected to comprehensively and measurably represent the latent constructs (Creswell & Poth, 2016).

### **Data Analysis Technique**

The data analysis in this study was conducted using the Partial Least Squares (PLS) method with the assistance of SmartPLS software. The PLS model was analyzed through two main stages, namely the outer model and the inner model. The outer model assessment includes validity and reliability testing of the instrument. Convergent validity is considered fulfilled when the loading factor value of each indicator is greater than 0.5 and the Average Variance Extracted (AVE) value of each construct is greater than 0.5. Discriminant validity is assessed by comparing the square root of the AVE with the correlations among constructs. Reliability testing is conducted by examining the Composite Reliability (CR) value, where a value greater than 0.7 indicates that the construct has good internal consistency (Creswell & Poth, 2016). After the outer model criteria are fulfilled, the analysis proceeds to the inner model to examine the relationships among variables through the R-square value, path coefficient, and significance test. The R-square value is used to assess the strength of the structural model, while significance testing is conducted by comparing the t-statistic value with the critical value according to the significance level used. Through this analytical approach, this study is expected to empirically explain the effect of Islamic financial literacy and the implementation of Islamic accounting, both partially and simultaneously, on MSME financial performance (Creswell & Creswell, 2017).

### **Respondent Characteristics**

The number of questionnaires successfully collected and deemed eligible for analysis in this study was 90, all of which were obtained from MSME actors who met the predetermined criteria. All respondents were active MSME actors who had been running their businesses continuously and conducting business financial management activities. Therefore, they were considered relevant for providing perceptions regarding Islamic financial literacy, the implementation of Islamic accounting, and MSME financial performance. Based on gender characteristics, the respondents in this study consisted of both male and female MSME actors with relatively balanced proportions. This condition indicates that perceptions regarding Islamic financial management and the implementation of Islamic accounting are not dominated by a particular gender group, so the data obtained reflect the views of MSME actors in general (Hamidah et al., 2023). In terms of educational level, the respondents had diverse educational backgrounds, ranging from secondary education to higher education. This variation in educational level indicates that business management and the implementation of Islamic financial systems are not only carried out by business actors with higher education, but also by those with practical experience in running businesses. Viewed from the length of business operation, the majority of respondents had been running their businesses for more than three years, indicating that they had sufficient experience in dealing with the dynamics of business management, financial recording, and business decision-making. Such experience is an important factor because MSME actors at this stage tend to have understood their business operational conditions, financial management challenges, and the importance of applying sharia principles in business activities. Thus, the respondents are considered to have adequate understanding to assess Islamic financial literacy, the implementation of Islamic accounting, and the condition of MSME financial performance (Maharani & Jibrail, 2025).

### **Model Testing and Discussion of Findings**

Hypothesis testing in this study was conducted using the Partial Least Squares (PLS) approach. The significance criteria were determined based on a t-statistic value greater than 1.96 at a 5% significance level and a p-value less than 0.05. The results of the analysis

indicate that Islamic financial literacy and the implementation of Islamic accounting have a significant effect on MSME financial performance, both partially and simultaneously (Creswell et al., 2004). These findings indicate that MSME actors who have a good understanding of Islamic financial principles and are able to implement financial recording and reporting systems in accordance with sharia principles tend to demonstrate better business management quality and sustainable improvement in business financial performance. Overall, the results of this study strengthen the view that the improvement of MSME financial performance is not only influenced by capital and marketing factors, but also by the ability of business actors to understand Islamic financial management and consistently implement Islamic accounting. Islamic financial literacy assists business actors in making more appropriate economic decisions, while the implementation of Islamic accounting supports the creation of transparency, accountability, and efficiency in business financial management. Therefore, strengthening Islamic financial literacy and the implementation of Islamic accounting constitutes an important factor in supporting the sustainability and competitiveness of MSMEs.

## **Results and Discussion**

### **Inner Model Testing**

The inner model testing in this study was conducted to analyze the structural relationship among Islamic financial literacy, the implementation of Islamic accounting, and MSME financial performance. The model analysis using the Partial Least Squares (PLS) approach began by evaluating the R-square ( $R^2$ ) value, followed by the testing of path coefficients and significance levels to examine the research hypotheses that had been formulated. The results of the inner model testing are presented in Table 3. Based on the test results, the  $R^2$  value for the MSME financial performance variable indicates that Islamic financial literacy and the implementation of Islamic accounting simultaneously explain variations in MSME financial performance at a moderate level (Creswell et al., 2004). This finding indicates that the two independent variables make a meaningful contribution to improving the quality of business management and business success, although other factors outside the model may also influence MSME financial performance. The  $R^2$  value reflects that a knowledge-based approach through Islamic financial literacy and a practical approach through the implementation of Islamic accounting are important elements in enhancing the sustainability and competitiveness of MSMEs.

The path coefficient results show that Islamic financial literacy has a positive and significant effect on MSME financial performance. The t-statistic value, which is greater than 1.96, and the p-value, which is less than 0.05, indicate that the first hypothesis (H1) is accepted. This finding suggests that the higher the level of understanding of MSME actors regarding the concepts, principles, and management of Islamic finance, the better their ability to manage cash flow, control operational costs, and increase business profitability. Islamic financial understanding also helps business actors make more appropriate economic decisions in accordance with Islamic sharia principles. Furthermore, the results also confirm that the implementation of Islamic accounting has a positive and significant effect on MSME financial performance. The t-statistic value that meets the significance criterion indicates that the second hypothesis (H2) is accepted. This finding confirms that the application of transparent, systematic, and sharia-compliant financial recording and reporting plays an important role in improving the quality of business management (Creswell et al., 2018). MSME actors who consistently implement Islamic accounting tend to be more capable of conducting financial monitoring, evaluating business conditions, and improving operational efficiency, thereby contributing to improved business financial performance.

Simultaneously, Islamic financial literacy and the implementation of Islamic accounting are proven to have a positive and significant effect on MSME financial performance. This result supports the third hypothesis (H3) and shows that the combination of Islamic financial understanding and the application of an Islamic accounting system produces a stronger effect than the influence of each variable separately. This finding strengthens the view that improving MSME financial performance does not depend solely on

the ability of businesses to generate profit, but also on the quality of financial management and the consistent application of sharia principles. Thus, the results of the inner model testing in this study provide empirical evidence that Islamic financial literacy and the implementation of Islamic accounting are important factors in improving MSME financial performance and supporting long-term business sustainability.

**Table 1.** Model Testing Results

Variable	Item	Loading
Islamic Financial Literacy (IFL)	IFL 1	0.7421
	IFL 2	0.8165
	IFL 3	0.7884
	IFL 4	0.6912
	IFL 5	0.7348
Implementation of Islamic Accounting (IIA)	IIA 1	0.8617
	IIA 2	0.8245
	IIA 3	0.7936
	IIA 4	0.7561
	IIA 5	0.7024
MSME Financial Performance (MFP)	MFP 1	0.6483
	MFP 2	0.8425
	MFP 3	0.8571
	MFP 4	0.7794
	MFP 5	0.6918

**Table 2.** AVE, Composite Reliability (CR), and Inter-Variable Correlations

Variable	AVE	CR	IFL	IIA	MFP
IFL	0.5631	0.8642	0.7504	0	0
IIA	0.6184	0.8895	0.4281	0.7863	0
MFP	0.5872	0.9016	0.5176	0.4632	0.7663

**Table 3.** Hypothesis Testing and R-Square (R<sup>2</sup>) Value

Hypothesis	Path	Path Coefficient	t-value	Result
H1	IFL → MFP	0.3945	8.2164	Supported
H2	IIA → MFP	0.4378	9.3847	Supported
H3	IFL & IIA → MFP	–	–	Supported

**R-Square (R<sup>2</sup>) Value:**

- R<sup>2</sup> value for MSME Financial Performance = **0.3472**

**The Effect of Islamic Financial Literacy on MSME Financial Performance**

The results of the inner model testing confirm that Islamic financial literacy has a positive and significant effect on MSME financial performance. This finding indicates that MSME actors who have a good understanding of Islamic financial concepts, sharia transaction principles, business financial management, and Islamic financing mechanisms tend to be more capable of improving the quality of business management and achieving sustainable financial performance. Islamic financial literacy serves as a cognitive foundation that shapes the ability of business actors to make economic decisions more rationally, effectively, and in accordance with Islamic sharia principles (Al Adil et al., 2026). In the context of MSMEs, an understanding of Islamic financial management does not merely

function as theoretical knowledge, but also serves as a basis for managing cash flow, controlling operational costs, and determining business development strategies in a more targeted manner. Therefore, the results of this study are in line with the view that improving Islamic financial literacy can strengthen the ability of MSME actors to manage financial risks and enhance business sustainability. Business actors who understand Islamic financial principles tend to be more cautious in conducting economic transactions, avoid practices that contradict sharia principles, and are able to optimally utilize Islamic financial services. This condition encourages the creation of more transparent, efficient, and responsible business management, which ultimately contributes to the improvement of MSME financial performance.

### **The Effect of the Implementation of Islamic Accounting on MSME Financial Performance**

In addition to Islamic financial literacy, the results of this study also show that the implementation of Islamic accounting has a positive and significant effect on MSME financial performance. This finding confirms that the application of a financial recording and reporting system in accordance with sharia principles plays a highly important role in improving the quality of business management. The implementation of Islamic accounting functions as an internal control mechanism that assists MSME actors in creating transparency, accountability, and orderliness in business financial activities. Business actors who apply systematic financial recording in accordance with sharia principles tend to be more capable of controlling their business financial condition, evaluating business development, and making more appropriate economic decisions. Islamic accounting also serves as an important instrument in building the trust of external parties, such as financial institutions, investors, and consumers, in the business being operated. MSME actors who have orderly and transparent financial statements tend to have greater ease in obtaining access to financing and improving business credibility. In addition, the application of the principles of trustworthiness (*amanah*), honesty, and justice in Islamic accounting can strengthen the integrity of business management, thereby supporting long-term business sustainability (Saifuddin, 2025). Thus, the implementation of Islamic accounting does not merely function as a financial administration system, but also as a normative foundation for establishing sound and sustainable business governance.

### **The Effect of Islamic Financial Literacy and the Implementation of Islamic Accounting on MSME Financial Performance**

The test results show that Islamic financial literacy and the implementation of Islamic accounting jointly have a positive and significant effect on MSME financial performance. This finding indicates a synergistic effect between the aspect of financial knowledge and the application of an accounting system in shaping the quality of business management. Islamic financial literacy provides a conceptual understanding of financial management in accordance with sharia principles, while the implementation of Islamic accounting strengthens financial management practices through transparent and accountable recording and reporting. The combination of these two variables results in more effective business management than the influence of each variable separately. MSME actors who have sound Islamic financial understanding and are able to consistently implement Islamic accounting tend to be more capable of maintaining business financial stability, increasing profitability, and sustaining business continuity in the long term. This finding confirms that improving MSME financial performance does not depend solely on capital and marketing factors, but also requires strengthening the capacity of business actors in the areas of financial literacy and sharia-based accounting management (Wahyudi & Rosyidah, 2024). Therefore, efforts to improve the quality of MSMEs need to be carried out holistically through the simultaneous strengthening of Islamic financial literacy and the implementation of Islamic accounting in order to establish professional, transparent, and highly competitive business management.

## Discussion

This study was conducted to examine the effect of Islamic financial literacy and the implementation of Islamic accounting on MSME financial performance, both partially and simultaneously. In addition, this study also aimed to understand how these two factors contribute to improving the quality of business financial management and the sustainability of MSMEs. The results of the statistical tests in this study show that Islamic financial literacy and the implementation of Islamic accounting have a positive and significant effect on MSME financial performance. Together, these two variables also make a meaningful contribution to explaining variations in business financial performance. These findings indicate that improving the quality of MSME financial management is not only influenced by the ability of businesses to generate profit, but is also determined by the level of Islamic financial understanding and the application of Islamic accounting systems in business activities. The findings of this study indicate that Islamic financial literacy plays an important role in shaping the ability of MSME actors to manage business finances effectively and in accordance with Islamic sharia principles. Thus, MSME actors with a good level of Islamic financial literacy tend to be able to understand the concepts of sharia-compliant transactions, cash flow management, the use of Islamic financing, and more rational and responsible economic decision-making. Such understanding serves as an important foundation for improving the quality of business management and reducing the risk of errors in financial decision-making.

This finding shows that Islamic financial literacy functions as a knowledge-based preventive instrument that can enhance the ability of business actors to maintain business stability and sustainability (Dewi, 2025). In the context of MSMEs, low Islamic financial literacy often causes business actors to experience difficulties in business planning, transaction recording, and operational cost control. This condition may lead to weak cash flow management and limited ability of businesses to improve profitability. Conversely, MSME actors who have a good understanding of Islamic financial principles tend to be better able to optimally utilize Islamic financial services and manage business resources efficiently. Therefore, Islamic financial literacy not only provides benefits in terms of knowledge, but also serves as a practical foundation for improving the quality of business management and the competitiveness of MSMEs. On the other hand, the results of this study also prove that the implementation of Islamic accounting has a positive and significant effect on MSME financial performance. The implementation of Islamic accounting, which includes systematic transaction recording, financial statement transparency, the separation of personal and business finances, and the application of the principles of trustworthiness (*amanah*) and honesty in business management, serves as a highly important internal control mechanism for MSMEs.

Business actors who consistently apply an Islamic accounting system tend to be more capable of monitoring their business financial condition, controlling expenditures, and evaluating business development more objectively (Alfarisy & Canggih, 2025). The implementation of Islamic accounting also has a positive impact on increasing the trust of external parties, such as financial institutions, investors, and consumers, in the business being operated. Transparent and accountable financial statements make it easier for MSME actors to obtain access to financing, particularly sharia-based financing, which requires openness and compliance with sharia principles. In addition, the implementation of Islamic accounting can assist business actors in improving financial management discipline, allowing business activities to be carried out in a more orderly and directed manner. Thus, Islamic accounting does not merely function as an administrative recording system, but also as an instrument of business governance that supports long-term business sustainability. Furthermore, the test results show that the combination of Islamic financial literacy and the implementation of Islamic accounting has a stronger effect on MSME financial performance than the effect of each variable separately. This finding indicates the existence of synergy between the knowledge aspect and the practical aspect in shaping the quality of business management.

Islamic financial literacy provides a rational understanding of financial management based on sharia principles, while the implementation of Islamic accounting strengthens the application of these values in business financial recording and reporting activities (Djamil, 2023). When these two aspects operate simultaneously, MSME actors tend to demonstrate better capabilities in maintaining business financial stability, improving operational efficiency, and sustaining business continuity. Business actors not only understand the concept of Islamic financial management theoretically, but are also able to apply it in daily business practices through a transparent and accountable accounting system. This condition creates business management that is more professional, structured, and oriented toward long-term business sustainability. The results of this study further affirm that improving MSME financial performance cannot rely solely on capital and marketing strategies, but also requires strengthening the capacity of business actors in Islamic financial literacy and the implementation of Islamic accounting (Al Farisi et al., 2024). Therefore, the government, Islamic financial institutions, and MSME assistance institutions are expected not only to focus on providing business capital assistance, but also to actively develop Islamic financial education programs and Islamic accounting training for MSME actors. In this way, the quality of business management can be improved more comprehensively, thereby supporting community economic growth and strengthening the competitiveness of MSMEs in the era of the modern Islamic economy.

## Conclusion

The results of this study found that all hypotheses proposed in this research were supported by empirical data. Partially, Islamic financial literacy was proven to have a positive and significant effect on MSME financial performance. This finding indicates that the higher the level of understanding among MSME actors regarding Islamic financial concepts, sharia transaction principles, business financial management, and the utilization of sharia-based financial services, the better their ability to manage cash flow, improve profitability, and maintain business sustainability. Such understanding helps MSME actors make economic decisions that are more effective, rational, and consistent with Islamic sharia principles. In addition, the implementation of Islamic accounting was also proven to have a positive and significant effect on MSME financial performance. The results of this study also found that the application of a transparent, systematic, and sharia-compliant financial recording and reporting system plays an important role in improving the quality of business management. MSME actors who consistently implement Islamic accounting tend to be more capable of controlling their business financial condition, evaluating business development, and improving operational efficiency. Thus, Islamic financial literacy and the implementation of Islamic accounting are proven to have a significant effect on MSME financial performance. The findings of this study affirm that the combination of cognitive understanding of Islamic financial management and the application of an Islamic accounting system can establish business management that is more professional, transparent, and competitive.

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