Effect of Financial Literacy, Reporting, and Risk Management on MSMEs Performance Mediated by Innovative Behavior

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ABSTRACT

The purpose of this study is to determine the influence of financial literacy, financial report preparation ability and risk management on financial performance. Types of quantitative research. The sample method used is nonprobability sampling with the Convenience sampling technique of 280 MSME respondents in Central Java. Financial literacy has been proven to have a positive effect on the financial performance of MSMEs. The ability to prepare financial statements has been proven to have a positive effect on the financial performance of MSMEs. Innovative behavior is able to mediate the relationship between financial literacy, and financial performance. Innovative behavior can mediate the relationship between the ability to prepare financial statements and financial performance.

Keywords: Financial Literacy, Financial Report, Financial Performance, Risk Management

Pengaruh Literasi Keuangan, Pelaporan, dan Manajemen Risiko terhadap Kinerja UMKM yang Dimediasi oleh Perilaku Inovatif

ABSTRAK

Tujuan penelitian ini adalah untuk mengetahui pengaruh literasi keuangan, kemampuan penyusunan laporan keuangan dan manajemen risiko terhadap kinerja keuangan. Jenis penelitian kuantitatif. Metode sampel yang digunakan adalah nonprobability sampling dengan teknik Convenience sampling sebanyak 280 responden UMKM di Jawa Tengah. Literasi keuangan terbukti berpengaruh positif terhadap kinerja keuangan UMKM. Kemampuan menyusun laporan keuangan terbukti berpengaruh positif terhadap kinerja keuangan UMKM. Perilaku inovatif mampu memediasi hubungan antara literasi keuangan, dengan kinerja keuangan. Perilaku inovatif dapat memediasi hubungan antara kemampuan menyusun laporan keuangan dengan kinerja keuangan.

Kata Kunci: *Literasi Keuangan, Laporan Keuangan, Kinerja Keuangan, Manajemen Risiko.*

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INTRODUCTION

Indonesia's economic growth cannot be separated from the role of Micro, Small and Medium Enterprises (MSMEs) which have an important and crucial role. MSMEs in Indonesia play a significant role in expanding and absorbing new workforce, contributing to the formation of Gross Domestic Product (GDP), and providing a safety net for low-income communities in carrying out productive economic activities. Indonesian MSMEs with a number of 99% of all business units contribute to GDP of 60.5%, with labor absorption of 96.9% of the total national labor absorption (Haryo LimansetoHaryo Limanseto, 2022). In 2023, the number of MSME business actors will reach around 66 million and is expected to increase to 83.3 million in 2024.

Although contributing to GDP and playing a crucial role in the regional economy, MSMEs often face challenges in achieving optimal financial performance, which can be grouped into two categories: financial problems and non-financial problems. Therefore, strategic efforts are needed to improve the financial performance of MSMEs. One way to achieve this is by enhancing the financial knowledge of MSME owners, so that their management and accountability can be better justified, similar to large companies.

MSMEs need to leverage every advantage they have to survive and grow. One approach that can be implemented is by understanding and applying the Resource-Based View (RBV) theory, which focuses on the development and management of specific and unique resources owned by the company, including: (1) Financial Literacy, (2) Financial Report Preparation Skills, (3) Risk Management, (4) Human Resources, (5) Innovation and Technology. The RBV theory becomes a key factor when determining competitive advantage, as it highlights the organization's need to produce, implement, utilize, maintain, sustain, formulate, and develop strategies (Asmolov & Ledentsov, 2022).

Previous research that discusses financial literacy with financial performance includes (Adella & Rio, 2021; Alamsyah Moh. Fuad, 2020; Dwinta Mulyanti & Ai Nurhayati, 2022; Dwiputri et al., 2023; Hartina, H., Goso, G., & Palatte, 2023; Septiani & Wuryani, 2020; Widiarti S, 2022) that financial literacy significantly affects the success or failure of small businesses. However, the exact influence of financial literacy on micro and small-scale business performance has not been fully identified, therefore this study is needed. The research was conducted by Dwiputri (2019) that innovative behavior is considered a moderator of financial literacy and financial risk and aversion to financial performance. The research outlines the ways that SME owners can improve their financial success by improving their financial literacy and embracing innovative behaviors that will ultimately benefit their businesses.

A previous study by Rahayu (2017b) stated that the performance of SMEs improves as financial literacy increases. A high level of literacy helps entrepreneurs be more cautious in their operations and makes management easier. According to Dwiputri et al. (2023b), the financial performance of SMEs improves when the owners have high financial literacy. Mulyanti & Nurhayati (2022b) also found that both financial literacy and financial technology, either partially or simultaneously, have a positive and significant impact on the financial performance of SMEs. Yunus et al. (2022b) revealed that financial literacy positively influences the financial performance of SMEs.

H1: Financial literacy has a positive effect on the financial performance of SMEs.

The ability to prepare financial statements can be viewed as a form of "intangible asset" according to the Resource-Based View (RBV), which includes knowledge and skills in processing and analyzing financial data. The study by Sukmana and Firmansyah (2014) revealed that the biggest issue in preparing financial statements in accordance with standards (SAK-ETAP) is the lack of professionalism among entrepreneurs and their unfamiliarity with SAK-ETAP. This study indicates that financial performance is influenced by the ability of SME entrepreneurs to prepare financial statements. Hernawati et al. (2019) explained that knowledge of financial statements affects the performance of SMEs.

H2: The ability to prepare financial statements has a positive effect on the financial performance of SMEs.

Research from economics, behavioral economics, and psychology fields has demonstrated that risk management, or uncertainty in decision-making, can impact financial performance (Boyle et al., 2012). The RBV emphasizes the importance of a company's internal resources and capabilities in creating sustainable competitive advantages (Barney, 1991b). These internal resources and capabilities can include physical assets, intellectual property, and skilled employees, so SMEs with effective risk management will influence decisions related to risk-taking and investment choices. These decisions, in turn, affect the financial performance of SMEs (Wong et al., 2018b). The relationship between risk management and financial performance, based on RBV, suggests that effective risk management can positively influence the financial performance of SMEs. By managing risk well, SMEs can reduce potential losses and increase potential gains, thereby improving their financial performance.

H3: Risk management in SMEs has a positive effect on the financial performance of SMEs.

Financial performance is an important activity to monitor the financial condition of a business, such as analyzing information from income statements, balance sheets, cash flow statements, and so on. Business owners and stakeholders can gain a deeper understanding of the financial situation. Innovation allows MSMEs to optimize business processes, reduce production costs, and improve operational efficiency, while also providing opportunities to collaborate with new business partners, expand business networks, and increase market visibility.

To enhance knowledge of financial literacy and financial digitalization, training is needed that includes understanding the benefits of financial digitalization, such as business bookkeeping in accordance with SAK EMKM standards, online payments, and engaging digital marketing. This foundation is used by the author as the population in the research, not only to determine the positive impact of the training provided, particularly financial literacy and business digitalization training, but also to explore how innovative behavior acts as a mediator for financial literacy, financial report preparation skills, and risk management in relation to the performance of MSMEs.

This study aims to analyze the effect of financial literacy, financial report preparation skills, and risk management on financial performance, as well as the performance of MSMEs in Central Java. Additionally, it seeks to analyze the mediating role of innovative behavior in the relationship between financial literacy, financial report preparation skills, and risk management on the financial performance of MSMEs in Central Java, leading to the following hypothesis:
H4b: Innovative behavior mediates the relationship between the ability to prepare financial statements and financial performance.
H4c: Innovative behavior mediates the relationship between risk management and financial performance.

RESEARCH METHOD

The population in this study consists of 925 MSMEs that have participated in the Financial Literacy and Financing Digitalization training organized by the Cooperatives and MSME Office of Central Java Province in 2023. The sampling method used is nonprobability sampling with a Convenience sampling technique, involving 280 MSME respondents in Central Java. The data used is primary data, with the dependent variable being financial performance and the independent variables being financial literacy, financial report preparation skills, and risk management, as well as the mediating variable being innovative behavior. Data analysis is conducted using descriptive statistics and Structural Equation Modeling (SEM) with a Partial Least Squares (PLS) approach.

RESULTS AND DISCUSSION

The respondent population is predominantly female in almost every category (age, education, and business duration). The most common age group among MSME owners is the productive age (40-55 years). The majority of owners have a secondary education (high school/vocational school), although there are also owners with a bachelor's degree (S1). Most businesses have been operating for more than 3 years, indicating business stability.

The *statistical T value* and P Value value are based on the results of *the Calculate PLS Bootstrapping* command in the following Table 1:

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Table 1. Statistical T *value* and *Exogenous P Value (Outer Loading) value*

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
X1_1 <- Financial Literacy	0.810	0.807	0.033	24.914	0.000
X1_2 <- Financial Literacy	0.754	0.747	0.049	15.265	0.000
X1_3 <- Financial Literacy	0.745	0.744	0.032	23.563	0.000
X1_4 <- Financial Literacy	0.781	0.780	0.033	23.617	0.000
X1_5 <- Financial Literacy	0.853	0.852	0.024	35.224	0.000
X1_6 <- Financial Literacy	0.824	0.822	0.030	27.408	0.000
X2_1 <- Ability to Arrange Financial _laporan	0.781	0.778	0.033	23.608	0.000
X2_10 <- Ability to Arrange Financial _laporan	0.854	0.853	0.025	34.709	0.000
X2_11 <- Ability to Arrange Financial _laporan	0.853	0.851	0.024	35.569	0.000
X2_12 <- Ability to Arrange Financial _laporan	0.789	0.788	0.033	23.576	0.000
X2_13 <- Ability to Arrange Financial _laporan	0.797	0.795	0.036	22.270	0.000
X2_2 <- Ability to Arrange Financial _laporan	0.794	0.793	0.030	26.410	0.000
X2_3 <- Ability to Arrange Financial _laporan	0.863	0.862	0.026	32.694	0.000
X2_4 <- Ability to Arrange Financial _laporan	0.879	0.878	0.020	43.875	0.000
X2_5 <- Ability to Arrange Financial _laporan	0.845	0.843	0.029	29.472	0.000
X2_6 <- Ability to Arrange Financial _laporan	0.867	0.867	0.025	34.542	0.000
X2_7 <- Ability to Arrange Financial _laporan	0.877	0.877	0.020	43.526	0.000
X2_8 <- Ability to Arrange Financial _laporan	0.872	0.873	0.021	42.303	0.000
X2_9 <- Ability to Arrange Financial _laporan	0.846	0.846	0.026	32.412	0.000
X3_1 <- Risk Management	0.827	0.827	0.025	32.922	0.000
X3_10 <- Risk Management	0.894	0.893	0.016	55.820	0.000
X3_11 <- Risk Management	0.887	0.887	0.020	44.891	0.000
X3_12 <- Risk Management	0.885	0.884	0.018	49.155	0.000
X3_13 <- Risk Management	0.872	0.870	0.022	39.772	0.000
X3_14 <- Risk Management	0.832	0.829	0.030	27.453	0.000
X3_15 <- Risk Management	0.887	0.887	0.019	47.394	0.000
X3_16 <- Risk Management	0.890	0.889	0.017	52.454	0.000
X3_17 <- Risk Management	0.894	0.895	0.017	52.857	0.000
X3_18 <- Risk Management	0.850	0.852	0.021	40.703	0.000
X3_2 <- Risk Management	0.826	0.824	0.033	25.115	0.000
X3_3 <- Risk Management	0.830	0.830	0.030	27.781	0.000
X3_4 <- Risk Management	0.820	0.818	0.039	21.155	0.000
X3_5 <- Risk Management	0.825	0.822	0.034	24.182	0.000
X3_6 <- Risk Management	0.810	0.807	0.048	16.799	0.000
X3_7 <- Risk Management	0.907	0.907	0.015	59.281	0.000
X3_8 <- Risk Management	0.907	0.907	0.013	71.533	0.000
X3_9 <- Risk Management	0.923	0.923	0.010	89.158	0.000

Source: Research Data, 2024

From the Table 1, the *statistical T* value ≥ 1.96 and *the P Value* ≤ 0.05 for all indicators and seen from the *Original Sample* value is all > 0.5, that is, so that no indicators are excluded from the model. As for the outer loading of endogenous variables, it can be seen in the Table 2.

Table 2. Statistical T *value* and *Exogenous P Value (Outer Loading) value*

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
Y_1 <- Financial Performance	0.824	0.823	0.027	30.776	0.000
Y_2 <- Financial Performance	0.784	0.782	0.029	26.809	0.000
Y_3 <- Financial Performance	0.858	0.857	0.023	37.403	0.000
Y_4 <- Financial Performance	0.729	0.727	0.034	21.275	0.000
Y_5 <- Financial Performance	0.719	0.720	0.040	17.891	0.000
Y_6 <- Financial Performance	0.861	0.860	0.027	31.529	0.000
Y_7 <- Financial Performance	0.787	0.783	0.032	24.246	0.000
Y_8 <- Financial Performance	0.752	0.748	0.029	26.036	0.000
Y_9 <- Financial Performance	0.852	0.849	0.027	31.067	0.000
Y_10 <- Financial Performance	0.793	0.790	0.036	21.999	0.000
Z_1 <- Innovative Behavior	0.862	0.862	0.027	32.443	0.000
Z_2 <- Innovative Behavior	0.844	0.843	0.036	23.760	0.000
Z_3 <- Innovative Behavior	0.897	0.897	0.021	43.211	0.000
Z_4 <- Innovative Behavior	0.889	0.888	0.020	43.484	0.000
Z_5 <- Innovative Behavior	0.855	0.852	0.034	25.010	0.000

Source: Research Data, 2024

From the results of the outer loading of endogenous variables, a *statistical T* value of ≥ 1.96 and *a P Value* of ≤ 0.05 for all indicators and *the original sample* > 0.5 so that all indicators are included in the model.

After calculating the validity value of the indicator, then through *Composite Reliability* (CR) and *Cronbach's Alpha* we look at *internal consistency reliability*. The minimum limit value of CR and *Cronbach's Alpha* is ≥ 0.7. In the following Table 3.

Table 3 CR. *Cronbach's Alpha,* AVE and R^2 values

	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
Ability to Arrange Financial _laporan	0.965	0.966	0.969	0.707
Financial Performance	0.936	0.938	0.946	0.636
Financial Literacy	0.883	0.888	0.911	0.632
Risk Management	0.980	0.982	0.982	0.749
Innovative Behavior	0.919	0.922	0.939	0.756

Source: Research Data, 2024

Data were obtained that the CR and *Cronbach's Alpha values* for all variables were ≥ 0.7, so it was concluded that the indicator was consistent in measuring the variables. *The Average* Variance Extracted (AVE) *value* of all variables is above > 0.50, then it can be stated that each variable has good discriminant validity. Meanwhile, the value of the Adjusted R *Square* (Adjusted R^2) value for each variable can be seen below.

Table 4. Adjusted R^2 Value

	R Square	R Square Adjusted
Financial Performance	0.759	0.756
Innovative Behavior	0.593	0.588

Source: Research Data, 2024

The Adjusted R *Square* (Adjusted R^2) value of 0.588 (58.8%) on the innovative behavior variable showed that the financial literacy variable, the ability to prepare financial statements and risk management could explain the innovative behavior variable by 53.7%. The Adjusted R *Square* (Adjusted R^2) value of 0.756 (75.6%) on the financial performance variable shows that the variables of financial literacy, ability to prepare financial statements, risk management and innovative behavior can explain the financial performance variable by 75.6%. The next construct reliability test is to evaluate the *discriminant validity* seen from *the cross loading value* and compare the root value of AVE with the correlation between variables. The cross *loading value* can be seen in the following table 5:

Table 5. Value *cross loading*

	Ability to Arrange Financial	Financial Performance	Financial Literacy	Risk Management	Innovative Behavior
X1_1	0.618	0.616	0.810	0.518	0.585
X1_2	0.550	0.533	0.754	0.531	0.449
X1_3	0.604	0.578	0.745	0.600	0.524
X1_4	0.624	0.565	0.781	0.549	0.541
X1_5	0.603	0.610	0.853	0.500	0.654
X1_6	0.651	0.618	0.824	0.476	0.623
X2_1	0.781	0.589	0.642	0.576	0.553
X2_10	0.854	0.681	0.690	0.649	0.631
X2_11	0.853	0.705	0.649	0.646	0.658
X2_12	0.789	0.650	0.625	0.610	0.576
X2_13	0.797	0.646	0.596	0.741	0.593
X2_2	0.794	0.600	0.601	0.505	0.523
X2_3	0.863	0.624	0.669	0.616	0.582
X2_4	0.879	0.654	0.687	0.678	0.609
X2_5	0.845	0.646	0.682	0.630	0.621
X2_6	0.867	0.643	0.651	0.668	0.605
X2_7	0.877	0.640	0.650	0.670	0.585
X2_8	0.872	0.672	0.633	0.653	0.598
X2_9	0.846	0.638	0.582	0.650	0.588
X3_1	0.617	0.526	0.514	0.827	0.531
X3_10	0.670	0.656	0.625	0.894	0.615
X3_11	0.700	0.665	0.611	0.887	0.615
X3_12	0.674	0.652	0.593	0.885	0.625
X3_13	0.680	0.657	0.580	0.872	0.600
X3_14	0.604	0.592	0.547	0.832	0.549
X3_15	0.671	0.624	0.593	0.887	0.607
X3_16	0.660	0.657	0.643	0.890	0.634
X3_17	0.673	0.687	0.639	0.894	0.644
X3_18	0.657	0.640	0.609	0.850	0.583
X3_2	0.635	0.534	0.504	0.826	0.494
X3_3	0.620	0.539	0.475	0.830	0.520
X3_4	0.622	0.497	0.489	0.820	0.457
X3_5	0.594	0.487	0.477	0.825	0.470
X3_6	0.599	0.557	0.523	0.810	0.529
X3_7	0.700	0.636	0.579	0.907	0.560
X3_8	0.716	0.659	0.603	0.907	0.600
X3_9	0.732	0.677	0.628	0.923	0.625
Y_1	0.648	0.824	0.591	0.593	0.656
Y_10	0.602	0.793	0.637	0.524	0.708
Y_2	0.613	0.784	0.593	0.534	0.722
Y_3	0.655	0.858	0.605	0.572	0.707
Y_4	0.509	0.729	0.515	0.530	0.630
Y_5	0.591	0.719	0.601	0.553	0.585
Y_6	0.687	0.861	0.603	0.663	0.704
Y_7	0.582	0.787	0.579	0.507	0.571
Y_8	0.558	0.752	0.475	0.554	0.552
Y_9	0.667	0.852	0.673	0.605	0.680
Z_1	0.639	0.746	0.657	0.587	0.862
Z_2	0.625	0.706	0.616	0.530	0.844
Z_3	0.636	0.767	0.642	0.608	0.897
Z_4	0.636	0.710	0.630	0.626	0.889
Z_5	0.532	0.626	0.544	0.524	0.855

Source: Research Data, 2024

The *cross loading* value above shows that all indicators have a greater correlation coefficient value with each variable compared to the correlation coefficient value with other variables/columns. This shows that each variable is well predicted by its indicators.

The next test is the correlation between the variables, as seen in the following table 6:

Table 6. Correlation Values Between Variables

	Ability to Arrange Financial	Financial Performance	Financial Literacy	Risk Management	Innovative Behavior
Ability to Arrange Financial _laporan	0.841				
Financial Performance	0.769	0.797			
Financial Literacy	0.765	0.739	0.795		
Risk Management	0.761	0.708	0.661	0.865	
Innovative Behavior	0.708	0.821	0.713	0.663	0.869

Source: Research Data, 2024

Based on the Table 6, it is known that variables, greater than the maximum value of the correlation between variables, indicate that other conditions *of discriminant* validity are met. The evaluation of the structural model will evaluate by looking at the significance of the relationship between variables (*Path Coefficient*) indicated by the *T value statistic* in the *Calculate PLS Bootstrapping* command in table 7 as follows:

Table 7. Nilai *Path Coefficient Direct Effect*

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
Ability to Prepare Financial _laporan -> Financial Performance	0.229	0.229	0.078	2.938	0.003
Ability to Construct Financial _laporan -> Innovative Behavior	0.254	0.257	0.107	2.380	0.018
Financial Literacy -> Financial Performance	0.145	0.141	0.063	2.284	0.023
Financial Literacy -> Innovative Behavior	0.369	0.366	0.078	4.753	0.000
Risk Management -> Financial Performance	0.124	0.128	0.053	2.331	0.020
Risk Management -> Innovative Behavior	0.226	0.225	0.079	2.878	0.004
Innovative Behavior -> Financial Performance	0.473	0.471	0.056	8.427	0.000

Source: Research Data, 2024

The results of the Table 7 show that *there is a* significant positive influence of financial literacy on financial performance in MSMEs in Central Java and the results align with the research hypothesis, where the hypothesis is accepted., meaning that the better the financial literacy, the higher the financial performance, resulting in *a T Statistic value* of 2.284 ≥ 1.96 and *a P Value* of 0.023 ≤0.05, shows that financial literacy improves financial performance, this shows that financial literacy refers to an individual's or business owner's understanding of the basic concepts and skills needed to make smart financial decisions. This includes the ability to manage budgets, understand financial statements, recognize risks, and plan investments.

The ability to prepare financial statements has a positive effect on the financial performance of MSMEs in Central Java, meaning that if the ability to prepare financial reports is better, then the financial performance will increase, resulting in *a T Statistic value* of 2.938 ≥ 1.96 and *a P Value* of 0.003 ≤0.05, showing that the ability to prepare financial statements is an important skill for MSME actors in managing and supervising the financial condition of their businesses in a timely manner. methodical. The test results align with the research hypothesis, where the hypothesis is accepted.

MSME Risk Management has a positive effect on the financial performance of MSMEs in Central Java, meaning that if risk management is better, then the higher the financial performance, resulting in *a T Statistic value* of 2.331 ≥ 1.96 and *a P Value* of 0.020 ≤0.05, indicating that better risk management has a crucial role in improving financial performance.

The evaluation of the structural model will evaluate by looking at the significance of the relationship between variables (*Path Coefficient*) *Indirect effect* shown by the *T value statistic* in the *Calculate PLS Bootstrapping* command in table 8 as follows:

Table 8. Nilai *Path Coefficient Indirect Effect*

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
Ability to Formulate Financial _laporan -> Innovative Behavior -> Financial Performance	0.120	0.121	0.051	2.368	0.018
Financial Literacy -> Innovative Behavior -> Financial Performance	0.174	0.173	0.043	4.074	0.000
Risk Management -> Innovative Behavior -> Financial Performance	0.107	0.106	0.039	2.735	0.006

Source: Research Data, 2024

Innovative behavior mediates the relationship between financial literacy and financial performance in MSMEs in Central Java, meaning that innovative behavior is able to strengthen or mediate the influence of financial literacy on financial performance, resulting in *a T Statistic value* of 4.074 ≥ 1.96 and *a P Value* of 0.000 ≤0.05, indicating that innovative behavior functions as an intermediary that connects financial literacy with financial performance. The test results align with the research hypothesis, where the hypothesis is accepted.

Innovative behavior mediates the relationship between the ability to prepare financial statements and financial performance in MSMEs in Central Java, meaning that innovative behavior is able to mediate the influence of the ability to prepare financial statements on financial performance, resulting in *a T Statistic value* of 2.368 ≥ 1.96 and *a P Value* of 0.018 ≤0.05, It shows that innovative behavior acts as an intermediary in the relationship between the ability to prepare financial statements and financial performance. This means that the ability to prepare good financial statements does not directly impact financial performance, but through innovative behavior.

Innovative behavior mediates the relationship between Risk Management and financial performance in MSMEs in Central Java, meaning that innovative behavior is able to mediate the influence of risk management on financial performance, resulting in *a T Statistic value* of 2.735 ≥ 1.96 and *a P Value* of 0.006 ≤0.05, indicating that innovative behavior acts as an intermediary in the relationship between risk management and financial performance. The test results align with the research hypothesis, where the hypothesis is accepted.

According to Mukarromah et al. (2020), financial literacy is the understanding of financial products and concepts with the help of information and advice, as well as the ability to identify and understand financial risks in order to make sound financial decisions. Financial literacy is a fundamental aspect that every individual must understand and master, as it influences one's financial condition and has an impact on making good and accurate economic decisions (Anggraeni, 2016).

Financial literacy has a positive effect on the financial performance of MSMEs because a better understanding of financial management allows MSME actors to make more informed decisions, optimize their resources, and increase the resilience and growth of their businesses. This leads to increased profitability and business sustainability in the long term. This is in line with previous research which states that if a person has good financial literacy, it will be able to improve performance (Moh Nur, Utomo, 2019). Research by Rahayu & Musdholifah (2017) said that the performance of MSMEs will increase along with the increase in financial literacy owned by their actors. Ariwibawa (2016) also said that the decisions taken by MSME actors related to finance must be accompanied by good financial literacy.

Financial statements help MSMEs track their expenses, income, and profitability on a regular basis. With the right financial records, business actors can understand their financial position clearly and take quick steps to address problems, such as financial leakage or inefficiency.

Financial statements provide concrete data that can be used to support business decision-making. MSME actors can use the information from financial statements to assess the performance of products or services, determine pricing policies, or decide whether it is feasible to expand their business. Decisions based on accurate data tend to be more precise and less risky. By compiling financial reports on a regular basis, MSMEs can identify business areas that need improvement. For example, they may find inefficient expenses or small profit margins. Business owners can immediately make adjustments, such as reducing production costs or optimizing resources, to improve overall financial performance. The ability to prepare financial statements also makes it easier for MSMEs to fulfill their tax obligations in a timely and accurate manner. Proper tax reporting can prevent businesses from fines or sanctions that could interfere with their financial performance. In Java, tax compliance is often an important issue in maintaining business sustainability. MSMEs that have good financial statements tend to be more competitive, because they can adjust more quickly to changes in market or economic conditions. With structured financial data, they can assess marketing strategies or product development more precisely, thereby increasing their competitiveness in local and regional markets.

Thus, the ability to prepare financial statements has a positive effect on the financial performance of MSMEs in Java because it allows business owners to have better control over their financial condition, make decisions based on valid data, better manage risks, and expand their access to external sources of financing. All of this supports the growth and sustainability of the business in the long term. This is in line with previous research with the RBV theory stating that the resources owned by companies are much more important than the structure of the industry in obtaining a competitive advantage (Barney, 1991). Related to the influence of the ability to prepare financial statements on the performance of MSMEs, it can be explained by Hernawati, Kuntorini, & Pramono (2019) that financial statement knowledge affects the performance of MSMEs.

By identifying risks early on, MSMEs can take preventive steps to minimize the negative impact of these threats. For example, the risk of loss due to fluctuations in raw material prices can be minimized by locking price contracts or making bulk purchases when prices are stable. Thus, good risk management can prevent MSMEs from significant financial losses. The market often undergoes changes, both in terms of consumer preferences and macroeconomic conditions. Effective risk management helps MSMEs prepare for this uncertainty. For example, MSMEs that mitigate risks by diversifying products or markets can be more stable when there is a decrease in demand in one segment. This adaptability keeps financial performance stable even in uncertain conditions. MSMEs that have a clear and planned risk management strategy tend to find it easier to get support from external parties, such as investors, creditors, or business partners. Investors and creditors see risk management as an indicator that MSMEs are able to manage their businesses wisely and maintain business continuity in the long term. This increases MSMEs' access to financing, which in turn has a positive impact on business development and financial performance. Natural disasters or pandemics, such as those experienced in several regions in Central Java, can have a significant impact on MSMEs. MSMEs that have a risk management plan, such as business insurance or a contingency plan, are better prepared to survive in an emergency situation. Thus, business continuity is more guaranteed, which directly contributes to the stability and improvement of their financial performance. Risk management also involves reviewing operational processes to identify potential inefficiencies.

Overall, **r**isk management has a positive effect on the financial performance of MSMEs in Central Java because it helps business actors anticipate and face various threats that can disrupt operations and finances. By minimizing potential losses, maintaining business continuity, and improving operational efficiency, MSMEs can maintain growth and financial stability in the long term. This is in line with previous research that Risk Management or uncertainty in decision-making will have an impact on financial performance (Boyle et al., 2012). Risk aversion is a term used to describe a person's tendency to prefer situations with more predictable outcomes but may have lower outcomes compared to situations that are highly unpredictable but potentially have higher outcomes (Dwiputri et al., 2023). MSMEs that have risk management will influence decisions in risk-taking and investment decisions. From this decision, it will affect the financial performance of MSMEs (Wong et al., 2018).

MSME actors who have good financial literacy are more sensitive to opportunities and challenges in their business. They are able to recognize areas where innovation is needed, such as cost management, new sources of income, or risk management. Financial literacy gives business actors the insight and confidence to try new approaches and be more daring to take measured risks. When business actors innovate, they can find more efficient ways to run their business, both in terms of production, distribution, and marketing. For example, innovations in marketing digitalization can expand the market, while innovations in stock management can reduce operational costs. Thus, innovation contributes directly to improving financial performance. Innovative behavior also allows businesses to continue to grow and adapt to market changes. An entrepreneur with good financial literacy and innovative behavior tends to be more flexible in dealing with economic changes, such as fluctuations in raw material prices or changes in consumer preferences. They can respond quickly and adaptively, thus maintaining or even improving financial performance in the midst of challenges.

MSME owners who have high financial literacy can realize that their profit margins are decreasing due to high distribution costs. With this understanding, owners innovate by looking for more efficient logistics solutions, for example using digital platforms for product delivery. This innovation not only reduces costs, but also opens up opportunities to reach a wider market. In this case, financial literacy triggers innovation, and the innovation then improves the financial performance of the business. Good financial literacy provides a solid foundation for business actors to make wiser financial decisions. However, in order for the impact of financial literacy on financial performance to be more optimal, business actors need to implement innovative behavior. Innovation allows business owners to utilize their financial knowledge in more creative and adaptive ways, thereby significantly strengthening financial performance. Thus, innovative behavior acts as a mediator that connects financial literacy and financial performance, where financial literacy encourages innovation, and innovation in turn improves financial performance. The results of the study are in line with the previous finding that innovative behavior is able to significantly strengthen the influence of financial literacy on financial performance (Ariwibawa, 2016; Dwiputri et al., 2023; Rahayu & Musdholifah, 2017).

When a business actor is able to prepare financial statements well, they can identify problems and opportunities in their business operations. For example, financial statements can reveal that production costs are too high or sales in certain segments are not optimal. From here, business actors can be encouraged to innovate, such as introducing new technologies to reduce production costs or developing new products to increase sales. Well-prepared financial reports provide in-depth information for business actors to make more targeted innovations. By having accurate financial data, they can be more confident in taking innovative risks that have the potential to increase revenue or efficiency. Once innovation is implemented, a positive impact on financial performance can be seen, such as increased profitability, reduced costs, or increased market share. Thus, innovative behavior is a factor that links the ability to prepare financial statements with improved financial performance.

MSME owners who are proficient in compiling financial statements see from the financial statements that profit margins have decreased due to high operational costs. Based on the data, he innovated by adopting digital technology to automate some of the business processes, which ultimately lowered operational costs and increased efficiency. This innovation then has a positive impact on the financial performance of the business. The ability to prepare good financial statements will provide business actors with clear information and insights about the financial condition of their business. However, in order for this insight to have a significant impact on financial performance, innovative behavior is needed. Innovation allows business actors to apply new ideas based on the financial statements, thereby improving or improving financial performance. In this case, innovative behavior acts as a mediator between the ability to prepare financial statements and better financial performance. The results of the study are in line with the previous finding that innovative behavior is able to significantly strengthen the influence of the ability to prepare financial statements on financial performance (Ariwibawa, 2016; Dwiputri et al., 2023; Rahayu & Musdholifah, 2017).

Innovative behavior acts as a mediator in the relationship between risk management and financial performance. In this case, good risk management will provide information and opportunities that can encourage innovative behavior in the company, and such innovation ultimately contributes to improving financial performance.

Innovations that are successfully implemented in response to risks can improve the company's financial performance. By innovating, companies can improve operational efficiency, expand markets, or find new ways to reduce costs. Continuous innovation also helps companies survive amid competition and market uncertainty, which ultimately has a positive impact on the company's profitability and financial stability. For example, a company engaged in the food industry faces the risk of supply chain disruptions due to the limitations of certain raw materials. Good risk management will help companies to anticipate these problems, such as by preparing alternative sources of raw materials or looking for new suppliers. In this process, the company can also innovate by using new processing technology that allows the alternative raw materials to be processed with the same quality. These innovations not only solve supply problems, but can also lower production costs, ultimately improving financial performance.

Good risk management provides a framework for companies to deal with and mitigate the impact of business risks. However, in order for risk management to truly have a significant impact on financial performance, innovative behavior is required. Innovative behaviors help companies respond to risk in more creative and adaptive ways, creating new solutions that have the potential to be profitable. In this case, innovative behavior becomes an intermediary factor that connects risk management and financial performance, where the innovations that emerge from good risk management can improve the effectiveness and efficiency of the company, which ultimately contributes to better financial performance.

Innovation allows companies to address risks in a proactive and creative way, and leverage challenges as opportunities to improve financial performance. The results of the study are in line with the previous finding that innovative behavior is able to significantly strengthen the influence of the ability to prepare financial statements on financial performance (Ariwibawa, 2016; Dwiputri et al., 2023; Rahayu & Musdholifah, 2017).

CONCLUSION

The scope of this study is limited to the factors of financial literacy, ability to prepare financial statement, and risk management on financial performance, with innovative behavior acting as a mediator. Other factors that may have a more significant impact are beyond the scope of this discussion, and it is expected that further research can be conducted based on existing studies.

Financial literacy has been proven to have a positive effect on the financial performance of MSMEs. The ability to prepare financial statements has been proven to have a positive effect on the financial performance of MSMEs. Innovative behavior is able to mediate the relationship between financial literacy, and financial performance. Innovative behavior is able to mediate the relationship between the ability to prepare financial statements and financial performance, which means that the ability to prepare good financial statements encourages innovative behavior that ultimately improves financial performance. Innovative behavior is able to mediate the relationship between Risk Management and financial performance meaning Effective risk management, when combined with innovative behavior, allows MSMEs to find new strategies in managing risk, which can strengthen their financial performance.

This study is expected to be developed within the scope of financial literacy programs that can be facilitated by institutions or the government, specifically for MSME owners. Further research is needed on the process of implementing basic accounting training for MSME owners, which includes risk management, how to prepare financial statements, as well as innovations in managing MSME businesses.

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