

Financial Performance Factors of MSMEs: An Analysis of the Mediating Effects of Government Support

^[1]Egga Adillah, ^[2]Friska Aditya

Faculty of Economics and Business, Universitas Panca Bhakti Pontianak

^[1]eggaadillah@gmail.com, ^[2]friskaaditya432@gmail.com

ABSTRACT

Micro, Small, and Medium Enterprises (MSMEs) play a pivotal role in the economic development of many countries, particularly in emerging economies. They contribute significantly to employment, income generation, and overall economic growth. However, despite their importance, MSMEs often face numerous challenges that hinder their financial performance and long-term sustainability. MSMEs are the cornerstone of the national economy, playing a vital role in driving economic growth. This study provides an in-depth analysis of how financial digitalization, Financial Inclusion, and access to Capital enhance the financial performance of MSMEs, focusing on the strategic role of government support as a mediating variable that strengthens these relationships. The type of research used in this research is quantitative, and the subject of this research is MSMEs in Pontianak City. The data analysis technique used is the Structural Equation Model (SEM) with the Smart PLS statistical test tool. The results of this study show that Financial digitalization and access to Capital positively impact MSME performance through government support as a mediator. However, government support cannot mediate the effect between financial Inclusion and MSME performance.

Keywords: Access capital; Financial digitalization; Financial inclusi; Government support

I. INTRODUCTION

MSMEs are the backbone of the national economy and play a crucial role in driving economic growth. This is evidenced by the MSME sector's contribution to the Gross Domestic Product (GDP), which accounts for 61%, and its contribution to employment, which reaches 97% of the total workforce (Perekonomian, 2023). The role of MSMEs is expected to increase further, in line with their strengths, enabling them to absorb more labor and withstand the challenges posed by the country's difficult economic conditions (Putra, Setiawan, Widyastuti, & Sari, 2023). MSMEs in Pontianak City are taking on a significant role in the sustainable development of MSMEs.

MSMEs in Pontianak City have experienced significant growth. Data shows that in 2021, the total number of MSMEs in Pontianak City was 41,573; in 2022, it was 41,878. And in 2023, the number of MSMEs increased to 43,247 (Koperasi UKM Provinsi Kalimantan Barat, 2022). Based on this data, it is essential to assess the financial performance of MSMEs in Pontianak City to ensure their sustained growth over time. Financial performance refers to the ability of MSMEs to operate efficiently, generate adequate income, survive, and grow by considering environmental opportunities and

threats (Risal, Wulandari, & Widyastuti, 2019).

In this era of rapid digitalization, MSMEs must adapt to technological advancements to seize the opportunities presented by digital technology for business development, ensuring sustainability and expanding market reach. Besides the rapid growth of digitalization, financial Inclusion and access to Capital are also vital components in improving the financial performance of MSMEs. Financial Inclusion refers to an individual's or company's access to various financial products, services, and institutions (Kristiawati, Giriati, Wendy, & Malini, 2024). Financial Inclusion enables MSMEs to access more financial services at affordable costs, thereby enhancing MSME performance (Kumar, Singh, & Dwivedi, 2020). The goal of financial Inclusion is to ensure that the community and MSMEs can access financial services such as loans, savings accounts, insurance, and payments, all of which are crucial for the sustainability and expansion of their businesses in the long term. A financially literate and confident community must be supported with access to financial institutions, products, and services (Kilay, Simamora, & Putra, 2022).

Government policies are critical for MSMEs to understand, as a lack of awareness and understanding of

current government policies can lead to MSMEs losing access to government support, resulting in setbacks and hindrances to business development. Based on interviews conducted by the researcher, it was found that many MSMEs still face challenges in utilizing financial digitalization, understanding financial Inclusion, and obtaining access to Capital. Additionally, government support is also a concern for the researcher. Several previous studies relevant to this research include the study (Hendratmoko, 2021), which states that digitalization influences improving MSME financial performance. Based on these findings, the researcher aims to examine further and analyze the impact of digitalization on MSME financial performance in Pontianak City.

In addition, the digitalization (Yunus & Siregar 2019) study shows that financial Inclusion affects MSME performance. In contrast, the survey (Almaidah & Endarwati, 2019) shows that financial Inclusion has a positive but insignificant impact, indicating that these studies still have inconsistent results. Access to Capital and government support are also areas of focus for the author, as the findings by (Sani et al., 2020) show that access to Capital has a positive and significant impact on MSME performance. However, these findings do not align with (Setiawan, Sari, Afif, Yahya, & Mayasafitri,

2024) findings. Additionally, the findings by (Tay, Tai, & Tan, 2022) regarding government policies reveal that government policies supporting MSMEs positively impact the growth of the MSME sector, while the findings by (Prataman, 2022) suggest that government policies do not affect MSME performance. These findings still show inconsistent results. The significant results of the impact of digitalization on MSME financial performance found by previous researchers have led the researcher to analyze further the influence of digitalization on MSMEs in Pontianak City. Meanwhile, the inconsistent results regarding financial Inclusion, access to Capital, and government policies on MSME performance found by previous researchers have prompted the researcher to investigate further to obtain more conclusive results on these inconsistent variables.

This study provides novelty by exploring the mediating role of government support in the relationship between financial performance factors and the financial outcomes of MSMEs, an area that has not been extensively investigated in previous literature. While many studies have addressed the direct impact of government support on MSME performance, few have examined how this support can mediate the relationship between internal and external factors affecting MSME financial performance. Thus,

this research offers a new perspective that has not been widely addressed in earlier studies. This research is expected to serve as a reference for policymakers in evaluating the effectiveness of support programs provided to MSMEs. By understanding its role, the government can tailor policies that are more adaptive and responsive to the actual needs of MSMEs, thereby enhancing the contribution of MSMEs to the overall national economy.

II. RESEARCH METHOD

This study employs a quantitative approach to test the formulated hypotheses regarding the influence of financial digitalization, Financial Inclusion, and access to Capital on MSME performance, with government support as a mediating variable. This research design was chosen because it is suitable for objectively measuring the influence between variables through data collection via questionnaires (Ghozali, 2016). The population for this study consists of MSMEs located in Pontianak City. The sampling technique used is purposive sampling. The minimum sample size is determined by multiplying the number of variables by the number of statement indicators, resulting in a minimum sample size of $5 \times 24 = 120$ samples. The data collection method used is a questionnaire, which was distributed both online and offline. The distribution of the questionnaires took place from May to June 2024. The data analysis technique used is square-structural equation modeling (PLS-SEM). The research model is presented in the following Figure.

H1: Financial digitalization has a positive impact on MSME performance.

H2: Financial Inclusion has a positive impact on MSME performance.

H3: Access to Capital has a positive impact on MSME performance.

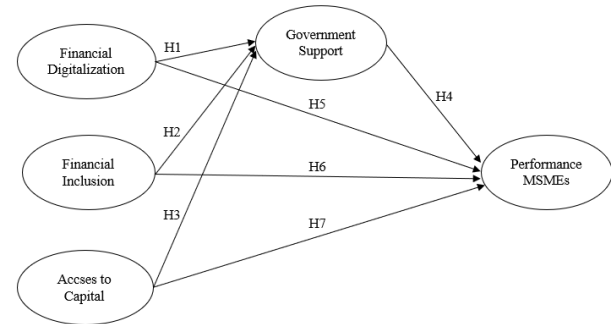


Figure 1. Research Model

H4: Government support has a positive impact on MSME performance.

H5: Financial digitalization positively impacts MSME performance through government support as a mediator.

H6: Financial Inclusion positively impacts MSME performance through government support as a mediator.

H7: Access to Capital positively impacts MSME performance through government support as a mediator.

III. RESULTS AND DISCUSSION

Results

Measurement Model. First, the individual reliability of the measurement scale is determined by analyzing the indicator loadings in reflective relationships. The required threshold value should be above 0.60 (Ghozali, 2016) and ideally above 0.70 (J. F. Hair, Sarstedt, Hopkins, & Kuppelwieser, 2019). Next, Cronbach's alpha and Composite Reliability (CR) are used to assess construct reliability. Cronbach's alpha represents the minimum threshold, while CR represents the maximum for internal

consistency reliability. The recommended value is 0.70–0.90 (J. Hair & Alamer, 2022). Table 1 describes the level of internal consistency for all accepted constructs.

Table 1. Measurement Model

Construct and Indicator	Loadings
<i>Access Capital (AC)</i>	
AC_1	0.721
AC_2	0.811
AC_3	0.851
AC_4	0.713
AC_5	0.665
AC_6	0.742
<i>Financial Digitalization (FD)</i>	
FD_1	0.806
FD_2	0.844
FD_3	0.845
FD_4	0.866
FD_5	0.760
<i>Government Support (GS)</i>	
GS_1	0.838
GS_2	0.857
GS_3	0.847
GS_4	0.843
<i>Financial Inclusion (FI)</i>	
FI_1	0.880
FI_2	0.817
FI_3	0.865
FI_4	0.816
<i>Performance MSMEs (P.MSME)</i>	
P.MSME_1	0.876
P.MSME_2	0.822
P.MSME_3	0.788
P.MSME_4	0.943
P.MSME_5	0.937

After evaluating reliability, convergent validity is checked using AVE, which must be higher than 0.5 (Fornell and Larcker, 1981).

Tabel 2. Crombach's Aplha, CR & AVE

Construct and Indicator	Crombach's Alpha	CR	AVE
Access Capital (AC)	0.851	0.942	0.766
Financial Digitalization (FD)	0.882	0.914	0.681
Government Support (GS)	0.868	0.910	0.716
Financial Inclusion (FI)	0.866	0.909	0.714

Performance MSMEs (P.MSME)	0.922	0.886	0.567
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All AVE values for each construct exceed 0.5, ranging from 0.567 to 0.766. The next step involves assessing discriminant validity using the Fornell–Larcker criterion. The square root of the AVE for each construct must exceed its correlation with other latent variables (Fornell and Larcker, 1981). The results indicate that the AVE value for each construct surpasses the construct's correlation. The obtained values remained below the established threshold, providing evidence of reliability and validity (see Table 2).

Table 3. Fornell-Lacker Criterion

Variable	(1)	(2)	(3)	(4)	(5)
AC	0.753				
FD	0.563	0.825			
GS	0.697	0.655	0.846		
FI	0.706	0.603	0.637	0.845	
P. MSME	0.833	0.730	0.816	0.766	0.875

The diagonal values represent the square roots of each construct's Average Variance Extracted (AVE), highlighted in bold, indicating the discriminant validity. Access to Capital has an AVE square root of 0.753. Financial Digitalization shows a high AVE square root of 0.825, with correlations to other variables, such as 0.563 with AC and 0.697 with GS. Government Support has an AVE square root of 0.846, indicating strong discriminant validity, with correlations of 0.655 to FD and 0.706 to FI. Financial Inclusion has a square root of AVE value of 0.845 and a correlation of 0.637 with GS. The performance of MSMEs demonstrates an AVE square root of 0.875, with the highest correlation (0.833) being with Access to Capital (AC). The table confirms that the square roots of the AVE for each construct are greater than their correlations with other

constructs, supporting the discriminant validity of the measurement model.

Results Hypotheses

Table 3 shows the results of assessing hypotheses with a one-tailed test, which is appropriate for coefficients with predicted signs (positive or negative) (Kock, 2014).

Table 4. Result Hypotheses

<i>Path</i>	β	<i>T-Value</i>	<i>p-values</i>	<i>Supported</i>
FD → MSME Performance	0.315	7.559	0.000	Yes
FI → MSME Performance	0.224	3.633	0.001	Yes
AC → MSME Performance	0.498	8.224	0.000	Yes
GS → MSME Performance	0.229	5.342	0.000	Yes
FD → GS → MSME Performance	0.102	3.759	0.000	Yes
FI → GS → MSME Performance	0.045	1.775	0.079	Yes
AC → GS → MSME Performance	0.119	3.581	0.000	Yes

The analysis results indicate that financial digitalization has a positive and significant impact on MSME performance, with a β value of 0.315, T-value of 7.559, and ρ -values of 0.000, which is below the cut-off value of 0.05 (J. F. Hair et al., 2019). This suggests that the higher the level of financial digitalization, the better the performance of MSMEs. Secondly, financial Inclusion also positively and significantly impacts MSME performance, with a β value of 0.224, T-value of 3.633, and ρ -values of 0.001. This result indicates that improving financial Inclusion can enhance MSME performance. Thirdly, access to Capital significantly impacts MSME performance, with a β value of 0.498, T-values of 8.224, and ρ -values of 0.000, indicating that better access to Capital can significantly improve MSME performance. Additionally, government support has been

proven to positively impact MSME performance, with a β value of 0.229, T-values of 5.342, and ρ -values of 0.000, confirming that government support is an important factor in enhancing MSME performance.

The mediation test results show that financial digitalization mediated by government support also significantly impacts MSME performance, with a β value of 0.102, T-value of 3.759, and ρ -values of 0.000. Similarly, access to Capital mediated by government support significantly impacts MSME performance, with a β value of 0.119, T-values of 3.581, and ρ -values of 0.000. These two findings confirm that government support strengthens the impact of financial digitalization and access to Capital on MSME performance. On the other hand, the data does not support the positive effects of financial Inclusion mediated by government support on MSME performance. The analysis shows a β value of 0.045, T-values of 1.775, and ρ -values of 0.079, above the cut-off value of 0.05 (J. F. Hair et al., 2019). This suggests that government support is not strong enough to mediate the impact of financial Inclusion on MSME performance significantly.

Discussion

Financial digitalization positively impacts MSME performance through government support as a mediator.

The research findings indicate that government support can mediate the impact of financial digitalization on MSME performance. Financial digitalization can directly improve MSME performance, such as using digital technology in transactions and financial management. However, this

effect becomes stronger when there is government support, such as policies that encourage the adoption of digital technology, training, or financial assistance for technology implementation. With this support, MSMEs not only find it easier to adopt digital technology, but they are also better equipped to utilize it to enhance efficiency, reduce costs, and access broader markets, ultimately improving their overall performance. These results underscore the importance of the government's role in creating a conducive environment for MSMEs to undergo digital transformation and optimize their potential in facing current economic challenges. The government has promoted cashless payments as concrete evidence of the application of digitalization in the trade sector. These cashless payments have increased transaction efficiency and reduced operational costs, allowing MSMEs to focus more on business development.

Financial Inclusion positively impacts MSME performance through government support as a mediator.

Government support cannot significantly mediate the impact of financial Inclusion on MSME performance. This means that while financial Inclusion, such as MSMEs' access to financial services, including loans, savings, and digital payments, can directly enhance MSME performance, government intervention or support has not successfully strengthened or mediated this influence. Recent research indicates that many government programs may be too general or not tailored to the specific needs of MSMEs across various sectors or regions (Akbar & Adi, 2022). Additionally, the low level of financial literacy among MSMEs may also

hinder them from effectively utilizing government support (World Bank, 2023).

Although the government has attempted to expand access to financial services through various initiatives, such as digitalization programs and interest rate subsidies, the results have not been sufficient to mediate the relationship between financial Inclusion and MSME performance (Lutfi et al., 2022). Many MSMEs still struggle to access formal financial services despite policy support due to barriers such as a lack of knowledge about available services or complicated administrative requirements (OECD, 2023). There is a need for better coordination between government policies and the specific needs of MSMEs, as well as the importance of improving financial literacy among small and medium business owners to ensure that government support can more effectively mediate the impact of financial Inclusion on MSME performance (Medhika, Giantari, & Yasa, 2018). Financial Inclusion may not be fully optimized to enhance MSME performance in Indonesia without a more targeted approach.

Access to Capital positively impacts MSME performance through government support as a mediator.

This study found that the impact of access to Capital on MSME performance can be strengthened through government support. The Institutional Support theory reinforces this finding by stating that the institutional environment, including government intervention, plays a crucial role in providing the necessary support to optimize the utilization of resources (Zahrah Buyong, 2020). Government support, such as interest

subsidies, credit guarantees, and MSME financing programs, creates more favorable conditions for MSMEs to access Capital (Lutfi et al., 2022). This allows MSMEs to obtain Capital on better terms, such as lower interest rates or more accessible requirements, enabling them to use that Capital more efficiently for business development.

The Resource-Based View (RBV) theory provides the foundation for understanding why access to Capital is vital for MSME performance. RBV posits that access to valuable, rare, and inimitable resources, such as Capital, is a key factor that enables companies to achieve competitive advantage and improve their performance (Barney, 1991).

This support helps MSMEs navigate challenges in accessing Capital, such as administrative barriers or high risks, which are often significant obstacles in this sector. The study emphasizes that government intervention in the form of institutional support is critical to maximizing the positive impact of access to Capital on MSME performance (Septiani N & Wuryani, 2020). Government support expands MSMEs' access to the resources they need and ensures that the Capital obtained can be optimized for business growth and sustainability. Without this support, the full potential of access to Capital to enhance MSME performance cannot be realized.

IV. CONCLUSION

The research findings indicate that government support can mediate the impact of financial digitalization and access to Capital on MSME performance. MSMEs not only find it easier to adopt digital technology,

but they can also utilize it to improve efficiency, reduce costs, and access broader markets, ultimately enhancing their overall performance. Government support expands MSMEs' access to the resources they need and ensures that the Capital obtained can be optimized for business growth and sustainability. However, government support cannot mediate the impact of financial Inclusion on MSME performance. Improving coordination between government policies and the specific needs of MSMEs and enhancing financial literacy among small and medium business owners is important to ensure that government support can more effectively mediate the impact of financial Inclusion on MSME performance.

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