

Enhancing Muslim SME Sustainability in Malaysia: The Role of Zakat and Financial Literacy

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Keywords

SME, zakat, financial literacy, financial management

Abstract

Financial literacy issues pose significant challenges for small and medium enterprises (SMEs) in Malaysia, leading to improper financial management practices and poor performance. In response to these challenges, this study explores the potential role of zakat, an Islamic fiscal tool, in addressing financial management issues among Muslim SMEs in Klang Valley. Specifically, the study analyses how zakat can serve as a mechanism for distributing targeted assistance to poor Muslim entrepreneurs within the SME sector. Motivated by zakat's potential to mitigate financial management and literacy issues, this qualitative study employed semi-structured interviews with seven Muslim SME owners to investigate the perceptions, experiences, and expectations surrounding zakat as a means of financial support tools for SMEs. Through thematic analysis, the study captured both common and nuanced insights related to zakat's role in strengthening financial management. The findings shed light on how zakat institutions can contribute to enhancing financial literacy and promoting sound financial management practices among Muslim SMEs, including the formulation of a proposed model of Non-Cash Zakat Distribution for Financial Management Services. This study also contributes to the literature by positioning zakat as a productive, developmental instrument within Islamic finance, rather than merely a form of direct aid. The implications of this study extend beyond the immediate context. By effectively leveraging zakat funds, policymakers, financial institutions, and zakat administrators can play a proactive role in supporting Muslim SMEs and promoting grassroots economic development.

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1. Introduction

Considering various economic developments in Malaysia since 2005, including price inflation, structural shifts, and evolving business trends, of the term ‘small and medium enterprise’ (SME) was reassessed in 2013 (SME Corporation Malaysia, 2013). Subsequently, a new definition was approved during the 14th National SME Development Council (NSDC) meeting in July 2013. This updated definition applies across all sectors, encompassing services, manufacturing, agriculture, construction, and mining and quarrying. It utilises two criteria – sales turnover and number of full-time employees – operating on an "OR" basis as outlined below:

a) For the manufacturing sector, SMEs are defined as firms with sales turnover not exceeding RM50 million OR number of full-time employees not exceeding 200.

b) For the services and other sectors, SMEs are defined as firms with sales turnover not exceeding RM20 million OR number of full-time employees not exceeding 75.

Diagram 1 provides the detailed definition of three categories: micro, small, and medium.

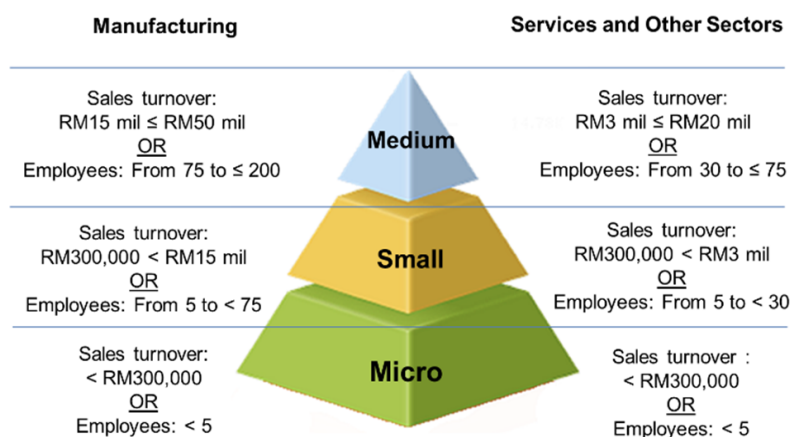


Figure 1. Definitions of micro, small, and medium enterprises, according to SME Corporation Malaysia, 2013.

In 2021, the global count of SMEs was roughly 332.99 million, showing a slight increase compared to the 2019 figure of 328.5 million (OECD, 2022). In Malaysia, too, SMEs play a pivotal role in the country’s economic landscape, constituting 97.4% of the 1,173,601 firms in Malaysia in 2022. There has been an increment of 87,068 firms as compared to a total of 1,086,533 Malaysian SMEs in 2016, thus

registering an average growth rate of 1.3% per annum during the period. Meanwhile, the performance of Malaysian SMEs remains favourable with outstanding growth in key macroeconomic indicators and contributed RM580.4 billion, or 38.4% of GDP, and offered employment opportunities to 7.59 million individuals (Department of Statistic, 2023). Over recent decades, Malaysia has established a robust financing framework comprising a range of funding avenues from both the public and private sectors, to cater to the diverse financial requirements of SMEs at different growth phases. This strategic approach ensures that Malaysian SMEs maintain access to varied financing channels, thereby facilitating their sustained development (OECD, 2022). For the Malaysian Budget 2024, the government allocated RM44 billion for credit facilities and funding guarantees specifically intended to support SME entrepreneurs. Out of the above amount, RM2.4 billion is assigned to agencies, including the central bank, commercial banks, and the National Business Enterprise Group Economic Fund (TEKUN), to support the growth and sustainability of SMEs (Hamid, 2023).

However, in terms of business size, the majority of Malaysian SMEs were microenterprises, comprising 78.7% (923,667 firms) of all SMEs in Malaysia (SME Corporation Malaysia, 2024). Meanwhile, small-sized firms accounted for 19.7% (231,546 firms), while medium-sized firms constituted the remaining 1.6% (18,388 firms). Between 2016 and 2022, there was an increase of 109,418 microenterprises, reflecting an average annual growth rate of 2.1%. Bumiputera-owned SMEs, which includes those owned by ethnic Malays and other indigenous peoples of Malaysia constitute 39.1% of the overall Malaysian SMEs landscape in 2020, with a significant proportion falling within the micro-sized category, as highlighted in the 12th Malaysia Plan (Teraju, 2021).

Zakat is an Arabic term that refers to an annual amount of surplus wealth, food, and/or property that Muslims with adequate means should distribute to fellow Muslims of lesser means, as mentioned in the Quran. Zakat, fundamentally understood as a form of worship (ibadah), is not merely perceived as a tax; rather, it fosters an understanding among Muslims that their wealth is entrusted to them by God. This perspective encourages them to share their resources with those who are less privileged as an expression of faith and devotion (De Zayas, 2003). Zakat serves the purpose of purifying the soul, promoting social assistance, and subsidising establishments and works of public welfare for the benefit and growth of the Islamic community. Zakat plays the role of mutual help in Muslim societies by eliminating poverty and bankruptcy in society, reducing inequality, helping

to redistribute wealth by creating social harmony and justice, and helping in the circulation of wealth from those well-endowed to the needy of society (Abdullah & Suhaib, 2011; Ibrahim, 2015). Prior studies by N. Hashim *et al.* (2020) and Rahman and Zulkarnain (2022) have examined the various forms of zakat provided by state governments and other institutions in Malaysia. However, research on non-cash zakat assistance in the form of financial education to increase financial literacy and financial management skills is lacking (Majlis Agama Islam Selangor, 2022).

The significance of financial management in SMEs cannot be overstated. Effective financial control is crucial for managing finances, cash, debts, investments, and working capital in SMEs. It also includes financial reporting, analysis, accounting information, inventory management, fixed asset management, and managing accounts payable and accounts receivable in various sectors in SMEs. The degree of performance of these firms is enhanced by improving the quality of managerial practices, as this improves the performance level and enhances SMEs' overall economic performance (Adjei-Boateng, 2022). Improved financial stability and growth can be achieved through proper financial management, which allows SMEs to access adequate finance, efficiently manage capital structure, and minimise the cost of funding (Jindrichovska, 2013). Proficient monetary management practices empower SMEs to make well-informed decisions, manage risks, and capitalise on growth opportunities (Mbaye *et al.*, 2023). Moreover, it fosters investor trust, attracts external investment, and sustains a competitive edge in the market (Hendayani *et al.*, 2022).

In today's data-driven business landscape, business analytics has emerged as a vital tool for organisations to extract insights from their existing data, enabling informed decision-making using artificial intelligence and machine learning technologies (Chidera Victoria Ibeh *et al.*, 2024). While large enterprises have wholeheartedly embraced business analytics as a strategic asset for operational enhancement, SMEs have been comparatively slower in adopting these transformative solutions. To remain competitive and surpass their rivals, SMEs must recognise the significance of harnessing their data assets effectively to drive decision-making processes (Windrum & Berranger, 2002). Therefore, leveraging digital technology to improve company decision-making requires efficient financial management and the timely availability of reliable financial data. Failure to address issues with financial management can impede the adoption and effectiveness of digital solutions, ultimately hindering the organisation's competitiveness and growth (Avira *et al.*, 2023).

However financial management remains a primary concern among Bumiputera entrepreneurs, the majority of whom are Muslim SME owners (A. Rahman *et al.*, 2023; Ayub *et al.*, 2020; Hashim *et al.*, 2020; Ishak *et al.*, 2012; Rahman & Zulkarnain, 2022). For instance, studies by Ishak *et al.*, (2012) and N. Hashim *et al.* (2020) found that Muslim SME owners often do not separate personal and business financial accounts, as they commonly use both interchangeably. These studies also suggest that most Muslim SME entrepreneurs only maintain basic transaction records, relying on limited financial knowledge (Ishak *et al.*, 2012). Furthermore, past research has revealed that a significant portion of Muslim SME owners lack proper systematic financial documentation and savings, indicating a lack of proficiency in accounting and cash management (N. Hashim *et al.*, 2020). These circumstances demonstrate the inadequate financial literacy among Muslim SME owners, which not only affects their accounting records but also poses critical risks, particularly during periods of economic crisis such as the COVID-19 pandemic, when about 90 percent of Bumiputera entrepreneurs, including SME owners, became at risk of bankruptcy due to various restrictions imposed during the pandemic (Khir, 2021). Moreover, the current economic challenges faced by Muslim entrepreneurs, including rising prices of goods, shortages of raw materials, and high bank loan interest rates, have led to increased operating costs for businesses (Hamid, 2023). Finally, the impact of poor financial literacy and management issues results in commercial banks lacking confidence in lending to these entrepreneurs (Omar *et al.*, 2015; Rahim *et al.*, 2019).

The existing literature highlights the importance of financial literacy for SMEs' sustainability and growth, which indirectly emphasises the need for investments in financial education initiatives. However, the financial support for financial literacy and financial management enhancement for Muslim SME entrepreneurs by zakat institutions is less explicitly discussed. Based on insights from the existing literature, it can be inferred that investing in financial literacy and providing financial support for literacy expenses can contribute to Muslim SMEs' success. Building on this foundation, this study aims to address the gap by investigating how zakat can actively support financial literacy and management among Muslim SMEs. While previous studies acknowledged the need for enhanced financial education, they lack a focused exploration of zakat as an Islamic tool within this domain. This study is important in examining the potential role of zakat, an Islamic fiscal tool, by conceptualising a non-cash zakat distribution model that enhances financial literacy, thereby positioning zakat as a productive instrument rather than merely

a form of charitable aid. By fostering sustainable growth and financial resilience among Muslim SMEs, this research contributes to Islamic finance literature and provides practical insights through the introduction of a sustainable and inclusive support mechanism for SMEs. This model aligns with Islamic finance principles, emphasising economic empowerment and the long-term sustainability of Muslim-owned enterprises. Ultimately, the study aims to underscore zakat's potential as a viable alternative solution to the capital challenges faced by SMEs, establishing a more inclusive and enduring financial support system within the Islamic framework.

2. Literature Review

2.1. Financial Literacy

The significance of financial literacy is well documented in recent literature. Financial literacy refers to the ability to understand basic principles of business and finance, as well as the knowledge and cognitive capabilities required to manage finances and make effective decisions on financial matters (Adomako *et al.*, 2016). Zait and Berteza (2014) identified the main dimensions of financial literacy, which are financial knowledge, financial abilities (capability to use financial information to make decisions), financial communication, financial behaviour, and financial confidence. In addition, research indicates that certain educational, cultural, and environmental variables contribute to the development of financial literacy (Grana-Alvarez *et al.*, 2022).

Thus, financial literacy is an important attribute not only for individuals but also for businesses as a management strategy to enhance competition and sustainable growth. For businesses, the key to success often lies in the company's owner or manager (Al-shami & Marwati, 2019). A study by Tang (2022), which examined 300 small enterprises in China, indicated that small business owners and managers must have financial literacy and possess essential financial management abilities to enhance the long-term sustainability of their firms. SME owners need financial literacy to evaluate their business's financial affairs, manage their resources and make wise financial decisions (S. Rahim & Balan, 2020). Financial literacy also helps businesses deal with challenges in cutting-edge credit markets and enable entrepreneurs to manage risks through strategies, such as maintaining financial reserves and diversifying their investment portfolio. Inadequate financial literacy has been identified as one of the main barriers to the sustainable development of SMEs (Ye & Kulathunga, 2019). Meanwhile, Kotze and Smit (2008) concluded that a lack of confidence in managing personal finance and an elevated degree

of financial literacy in managing finance can lead to the potential failure of new ventures in SMEs.

2.2. Muslim SMEs and Sustainability

SMEs are one of the main components of the economic system. They are indispensable for maintaining the sustainability of economic activities (Masdupi *et al.*, 2024). Yet, their sustainability hinges on effective financial management, which is inherently linked to the level of financial literacy among owners and managers (Al-shami & Marwati, 2019). Previous studies consistently underscored the critical role of financial literacy in SME sustainability (Masdupi *et al.*, 2024; Seraj *et al.*, 2022; Top & Özbek, 2022). Masdupi *et al.* (2024) emphasised that inadequate financial literacy leads to inaccurate financial decisions, while Tian *et al.* (2022) and Sharma (2022) highlighted financial literacy's positive impact on corporate performance and business growth. Furthermore, financial literacy contributes to improved financial management practices, access to finance, risk mitigation, and transparency, thereby fostering long-term sustainability (Eniola & Entebang, 2017; Tian *et al.*, 2022).

Despite the significance of financial literacy, several challenges hinder its integration into SME operations. These challenges include limited access to financial education programmes, cultural barriers, and a lack of awareness regarding the importance of financial literacy (Damayanti *et al.*, 2018; Mutamimah & Indriastuti, 2023). Additionally, the effectiveness of financial literacy initiatives may be constrained by varying levels of educational attainment among SME owners and managers. Moreover, the shortcomings encompass the requirement for continuous learning and instruction, in addition to the difficulty of integrating academic understanding into practical commercial situations. The success of financial literacy programmes may also be impacted by contextual and cultural factors (S. Rahim & Balan, 2020). The association between SMEs' sustainability and financial literacy is influenced by several moderating and mediating factors. The moderating effect of generational stages on the connection between company growth and CEO financial literacy in family-owned SMEs is highlighted by Diéguez-Soto *et al.* (2022). On the other hand, there is a mediating role for organisational risk-taking tolerance in the link between financial literacy and SME sustainability (Masdupi *et al.*, 2024). Further partial mediators of the complex interactions determining SME sustainability are the financial risk mindset and availability of financing (Ye & Kulathunga, 2019). Finally, Al-shami and Marwati (2019), concluded that the factors affecting financial literacy for SME owners or managers can be

summarised in three dimensions: financial knowledge (education, experience, perception and opinion, knowledge product and service, socialisation agents), financial attitude (money attitude, expenditure, income level), and financial awareness (saving and investment, retirement plan).

To advance the understanding in this field, past studies have suggested that future research should focus on addressing several key areas. Firstly, there is a need for longitudinal studies to examine the long-term impact of financial literacy interventions on SME sustainability. Secondly, exploring innovative approaches to financial education delivery, such as digital platforms and peer-to-peer learning networks, could enhance accessibility and effectiveness. Additionally, comparative studies across different cultural and socio-economic contexts would provide valuable insights into the generalisability of findings. Moreover, investigating the role of emerging financial technologies in enhancing financial literacy and SMEs' sustainability merits attention (Winarsih *et al.*, 2024). A recent study examining the factors influencing the financial sustainability of 285 Bumiputera SMEs in the food processing industry in Selangor revealed that these enterprises exhibit low levels of financial literacy. To address this issue, the study recommends leveraging government-provided financial literacy assistance and advisory services, as well as implementing mentoring programmes with larger enterprises to enhance the financial literacy of Bumiputera SMEs (A. Rahman *et al.*, 2023).

2.3. Zakat and Its Role in Supporting SMEs

Zakat distribution is a fundamental aspect of Islamic economic and social welfare systems. It involves the collection and redistribution of obligatory alms from Muslims who are financially capable, known as zakat payers (muzakki), to those in need, referred to as zakat recipients (mustahiq) (Wahid, 2009). *Asnaf* is a group that Allah has determined eligible to receive alms aid (Mohd *et al.*, 2021), while zakat institutions are the organisations in charge of zakat collection and distribution. Zakat funds are allocated to eight categories of Muslims as mentioned in the Quran: the hardcore poor, referring to those who either have no assets or income, or whose resources amount to less than half of the basic subsistence level (fakir); the poor, who have a level of wealth or income that meets more than half of the basic subsistence level but remains below the threshold required to achieve full subsistence (miskin); zakat operators, who are the individuals appointed by zakat institutions to administer the collection and distribution of zakat funds (amil); individuals who have recently become inclined to Islam (muallaf); slaves, referring to those who are constrained by certain forces or conditions that hinder their

ability to lead a better life (riqab); debtors, referring to those who are facing a debt burden without sufficient means to repay (gharimin); wayfarers who are fighting in the way of Allah (fisabilillah); and travellers who are stranded or in need during their journey (Ibnu Sabil). The poverty groups and wayfarers are the top priority of Malaysian zakat institutions, while debtors, slaves, and travellers are given the least importance (Azhar *et al.*, 2023; Muhamad *et al.*, 2018).

In principle, zakat assistance is divided into two forms: consumptive zakat distribution and productive zakat distribution. Consumptive zakat distribution entails direct assistance to *asnaf*, and productive zakat distribution involves acquiring assets for *asnaf* for their specified use or providing capital to *asnaf* for further development. Therefore, assistance to SMEs is categorised as productive zakat (Hambari *et al.*, 2020). In a study by N. Hashim *et al.* (2020) focusing on micro-sized business entrepreneurs who received assistance from Kedah Zakat. Kedah Zakat, one of the fourteen zakat institutions in Malaysia operating under state jurisdiction, is mandated to oversee the management of zakat collection and distribution within the state of Kedah. N. Hashim *et al.* (2020) found that *asnaf* entrepreneurs encounter challenges such as a lack of skills and knowledge in business management, particularly in financial aspects, as well as in the operation of production and marketing activities. To overcome these challenges, the study suggested the implementation of structured entrepreneurship programmes to enhance participants' business management efficiency and effectiveness. These programmes should include elements such as physical and financial support, training in entrepreneurial functions, periodic motivation, monitoring, and support and could be executed in collaboration with existing government agencies and communities. Ultimately, such initiatives aim to uplift *asnaf* entrepreneurs from poverty and facilitate their progression towards becoming zakat contributors in the future (N. Hashim *et al.*, 2020).

Research by Rahman (2022) examined initiatives implemented by several zakat institutions during the COVID-19 pandemic in Malaysia. The types of initiatives done by the zakat institutions in helping SMEs from the *asnaf* group are shown in Table 1.

Table 1. Initiatives of Zakat Institutions

No	Institution of Zakat	Initiative
1.	Lembaga Zakat Selangor (LZS)	- RM 12.1 million COVID-19 assistance to B40* hawkers/traders & workers whose income were affected - Program <i>Pemeriksaan Usahawan dan Transformasi Pembangunan Inovatif</i> for <i>asnaf</i> entrepreneurs (Zainury, 2021).

2.	Pusat Pungutan Zakat - Majlis Agama Islam Wilayah Persekutuan (PPZ-MAIWP)	- An allocation of RM15 million for the new aid, Musa'adah Tijariyyah, which targeted 5,000 recipients (MAIWP, 2022). - SME Corporation Malaysia (SME Corp) collaboration organised the Tunas Usahawan Baitulmal (TUB) programme (BERNAMA, sd). - Majlis Agama Islam Wilayah Persekutuan (MAIWP) and Yayasan Pembangunan Ekonomi Islam Malaysia (YaPEIM) allocated RM3 million to assist entrepreneurs from the <i>asnaf</i> group to cope with the challenges of the COVID-19 pandemic (Khair, 2021).
3.	Majlis Agama Islam dan Adat Istiadat Melayu Perlis (MAIPs)	- Bantuan Khas Rangsangan <i>Asnaf</i> in the form of exemption for rental of houses, shops and bazaars for a period of three months, worth RM 343,317 (MAIPs, 2020).
4.	Majlis Agama Islam dan Adat Istiadat Melayu Kelantan (MAIK)	- Financial assistance ranging from RM300 to RM500 to 19,000 traders affected by COVID-19
5.	Lembaga Zakat Negeri Kedah Darul Aman (LZNK)	- Distribution of Skim Bantuan Perniagaan/Jayadiri worth RM1.8 million in 2021 and RM1.4 million in 2020.
6.	Majlis Agama Islam dan Adat Melayu Perak (MAIPK).	- Special Assistance of Small Entrepreneurs Revolving Capital of RM2 million (MAIPK, 2021). - Implemented the <i>Asnaf</i> Capital Assistance Scheme (ABaM) (MAIPK, 2021). - Organised the Bengkel Pembentukan Model Perniagaan Usahawan <i>Asnaf</i> dan Kajian Keberkesanan Program Pemerkasaan Ekonomi <i>Asnaf</i> (Proper A) (MAIPK, 2020).
7.	Zakat Pulau Pinang (ZPP)	- Special assistance to small traders and hawkers affected by the spread of the COVID-19 pandemic on 23–28 March 2020. - Skim Bantuan Khas COVID-19 (SKBC19) to 672 traders in night markets/farmers' markets or small entrepreneurs amounting to RM336,000 in 2021 (Zakat Pulau Pinang, 2021). - Transformasi Minda Usahawan course organised by Zakat Pulau Pinang (Zakat Pulau Pinang, 2021). - Transformasi Minda Usahawan course organised by Zakat Pulau Pinang (Zakat Pulau Pinang, 2021).
8.	Pusat Kutipan Zakat Majlis Ugam Islam Pahang	- Established the BizZakat Portal as a business platform (Awang, 2021). - A donation of RM1,000 to each <i>asnaf</i> entrepreneur (Abdul Rahman, 2021).
9.	Majlis Agama Islam Negeri Johor (MAINJ)	- Provided training on how to run a business, including hair cutting (Ali, 2020). - Online marketing in collaboration with Johor Bizz Digital (Ali, 2020).

*Note: The term B40 generally refers to the bottom 40% of income earners in a given population or society. It is often used in socioeconomic and policy contexts to identify and address issues faced by low-income groups. In Malaysia, the B40 group is officially recognized and often contrasted with other income groups such as the M40 (Middle 40%) and T20 (Top 20%). The government uses these classifications to direct subsidies, housing programs, healthcare, and other welfare initiatives to the B40 group

Based on Table 1, there are three main types of zakat institution initiatives:

1. Financial assistance in the form of capital and one-off cash payments.
2. Provision of comprehensive training by state zakat institutions or in cooperation with other bodies.
3. Provision of business platforms, including exemption of premise rental fees.

In the state of Selangor, entrepreneurial assistance is provided to three

categories of *asnaf*, encompassing various types of aid (Table 2).

Table 2: Types of Zakat Assistance by *Asnaf* Categories

<i>Asnaf</i> Category	Types of Zakat Assistance
<i>Fakir</i> (The Poor)	- <i>Asnaf</i> Project - Training/Courses
<i>Miskin</i> (The Needy)	Sewing Workshop Management <i>Mawaddah Kraf</i> (Recycling waste into handmade products) Capital Assistance - Business Capital Assistance - Fishery Capital Assistance - Cattle Capital Assistance - Agriculture Poverty Trust Fund (Group Capital) Training/Courses
<i>Muallaf</i>	Capital Assistance Training/Courses

Lembaga Zakat Selangor (Selangor Zakat Board) distributed a total of RM12.2 million to 1,288 *asnaf* entrepreneurs to support business development and enhancement in 2022. Of this figure, 813 *asnaf* entrepreneurs were categorised as having potential, while the number of successful Muslim entrepreneurs categorised as successful in the same year was 119 individuals (Majlis Agama Islam Selangor, 2022). Collectively, the studies reviewed here identify the various forms of cash and non-cash zakat.

3. Methodology

The research design adopted for this study is a basic qualitative approach. It aims to understand how individuals interpret their experiences and to gain insights into the perceptions, experiences, and expectations regarding the utilisation of zakat as a financial support tool for Muslim SMEs in Malaysia. The study utilised in-depth interviews to gather evidence. This method allows for a detailed exploration of issues and provides compelling insights based on human experiences, which are often more persuasive than quantitative data (Rahman; M. S., 2017). By conducting in-depth interviews, the researcher can capture participants' experiences, perspectives, and beliefs related to a specific research question or phenomenon of interest (Ryan *et al.*, 2009).

The researcher utilised a purposive sampling approach to select participants who voluntarily agreed to take part in the study. Seven semi-structured interviews

were conducted, with data collection continuing until saturation was reached, ensuring that no new themes emerged from additional interviews, as guided by Creswell's (1998) recommendation of between five and 25 interviews for phenomenological research. The interviewees included Muslim business owners and directors actively engaged in SME operations in the Klang Valley (Kuala Lumpur, Putrajaya, and Selangor).

The researcher conducted face-to-face interviews with the participants in March 2024. The focus was on the perceptions and experiences of Muslim SME owners and directors regarding financial management and literacy, as well as their expectations regarding zakat as a financial support tool for Muslim SMEs. A semi-structured interview approach was employed, with initial questions extended as necessary based on the discussion flow. The researcher observed the respondents' responses to the questions raised. Thematic analysis was utilised, involving transcription of interview recordings and subsequent coding stages. Data obtained from the interviews was transcribed to understand the interviewees' responses and contextual nuances before undergoing coding to organise text segments into meaningful units to facilitate analytical interpretation. Before identifying the final themes, the researcher repeatedly reviewed transcripts to identify potential themes aligned with the research aims.

4. Results and Discussion

The profiles of the respondents are summarised in Table 3.

Table 3. Characteristics of Interview Participants

Respondents	Gender	Years of Experience in SMEs	Education Background (Highest Qualification)	Head Office Location	Zakat Recipients	Nature of Business
R1	Male	10	Degree	Shah Alam, Selangor	No	Construction
R2	Male	8	Degree	Kuala Lumpur	No	Construction
R3	Female	14	Secondary School	Kuala Lumpur	Yes	Tailor Shop
R4	Male	16	Secondary School	Kuala Lumpur	Yes	Food Truck
R5	Male	30	PhD	Gombak, Selangor	No	Education Consultation
R6	Female	15	Master	Cyberjaya, Selangor	No	Sport and Fitness
R7	Male	6	Master	Putrajaya	No	Laundry

The results of the thematic analysis of the interviews were presented under the following six emergent themes:

1. Level of Financial Literacy Understanding
2. Challenges in Acquiring Financial Literacy and Management Knowledge
3. Significance of Financial Literacy
4. Impact on Financial Sustainability
5. Government/Zakat Assistance
6. Zakat Assistance: Bridging Financial Literacy and SME Sustainability.

4.1. Level of Financial Literacy Understanding

The findings of past studies indicated that the primary challenge faced by many Muslim SME owners is understanding financial literacy to manage their businesses (Rahman *et al.*, 2023). The concept of financial literacy encompasses a broad definition scope, extending across various areas such as budget management, savings, investments, debt management, accounting, and costing. In assessing respondents' understanding of the concept of financial literacy, all respondents generally described financial literacy as related to financial management and accounting. One interesting finding regards the concept of financial literacy in managing company finances wisely and prudently:

“Financial literacy is the ability to understand and manage finances in spending, budgeting, saving and investing wisely.” (R4)

Another perspective considers financial literacy to encompass aspects of compliance with financial statement reporting and auditing:

“Maintain financial records of the company, generate financial reports, and submit financial information for audit and project costing purposes.” (R6)

This indicates a very broad interpretation of financial literacy. In general, the definition of financial literacy extends beyond direct financial management to encompass critical thinking about opportunities and threats before making informed decisions to enhance business effectiveness (Molina-García *et al.*, 2023). This condition will pose challenges for SME owners, most of whom have limited financial resources and a relatively low number of employees. This is because proficiency in managing company finances encompasses a wide array of financial aspects that significantly influence both time and costs.

In line with the observations, four respondents rated their knowledge at a

moderate level, while three others achieved advanced scores. However, two respondents with advanced knowledge levels were zakat recipients with 14 to 16 years of business experience. Additionally, another respondent with advanced financial literacy had 30 years of experience in SME management. This situation indicates that business experience is a crucial factor in determining the level of financial literacy among SME owners. Furthermore, the zakat recipients rated their financial literacy level as advanced due to zakat assistance provided by zakat institutions in Malaysia, which includes not only business capital assistance but also courses and training related to business management, including financial management.

4.2. Challenges in Acquiring Financial Literacy and Management Knowledge

In managing SMEs, seven respondents identified several key challenges in acquiring knowledge related to financial literacy and financial management. Among the main challenges faced by SMEs are the tendency of SME owners to focus only on business operations (R1, R6), insufficient staffing for conducting effective financial management while preventing cost escalation within the company (R2), inadequate awareness of institutions providing expertise in financial literacy (R4), and total dependence on appointed employees to handle financial matters (R7).

*“Especially those with a technical background, the majority of business owners lack financial knowledge prior to establishing their companies. They were **more concerned with their core operation.**” (R1)*

The study findings also indicate that the issues faced not only involve SMEs' inability to provide sufficient funds and manpower to manage finances but also their lack of information or access to enhanced knowledge and skills to manage financial matters (R4).

*“Didn't know the right place to get exposure and knowledge of finance and **how to manage resources.**” (R4)*

The selection of programmes to enhance the level of knowledge and skills in financial literacy is crucial to ensure that attended programmes have an effective impact. This is because the approach implemented by some of the existing training programmes does not have an effective impact on improving financial literacy (Yakob et al., 2021).

Furthermore, cultural attitudes towards financial management may influence SME owners' willingness to prioritise financial literacy education (Damayanti et

al., 2018). Cultural attitudes towards money, risk-taking, and financial practices shape entrepreneurs' behaviour. For instance, some cultures prioritise saving and conservative financial management, while others may encourage entrepreneurial risk-taking and investment. These differing cultural perspectives can influence entrepreneurs' decisions on savings, investments, and debt management, impacting their financial literacy and decision-making processes. Therefore, SME owners should seek opportunities to enhance their financial knowledge and skills. This is to ensure that they can manage their companies more effectively and sustainably, resulting in sustainable profits.

4.3. Significance of Financial Literacy

Financial literacy is undeniably critical for the success and sustainability of SMEs. In today's dynamic business environment, where economic uncertainties and market complexities abound, SME owners must possess a solid understanding of financial management principles to navigate challenges effectively and drive business growth.

In discussing the objectives of implementing good and orderly financial management, all respondents agree that efficient and effective financial management is crucial to achieving the company's targeted objectives. Additionally, respondents concur that good financial management can streamline operations (R1), enhance company growth (R3, R5, R6), improve stability and sustainability (R2, R5), provide essential input for strategising and decision-making (R4, R7), and that detailed information and analysis conducted through financial management helps SME owners assess company performance (R7).

*“Yes, among the **causes of business failure is as a result of difficulties with financial management** due to lack of financial literacy.” (R3)*

In the realm of SME ownership, the question of whether to engage external consultants versus fostering in-house financial expertise for the preparation of company accounts is a matter of considerable debate. On one hand, proponents of outsourcing argue that tapping into external expertise can provide SMEs with specialised knowledge and resources, potentially leading to more accurate financial reporting and strategic financial decision-making. Conversely, advocates for developing in-house capabilities argue that cultivating internal talent fosters greater control, responsiveness, and understanding of the company's financial operations (Harpal S., 2023). Those in favour of engaging consultants often cite the complexity and technicality of financial reporting requirements as the

primary reason. SME owners, especially those with limited financial acumen, may find it challenging to navigate the intricacies of accounting standards, auditing requirements, tax regulations, and financial analysis. By outsourcing these tasks to professionals, SMEs can ensure compliance, accuracy, and timeliness in financial reporting, thereby avoiding costly errors and penalties.

*“Depends on type of business. **Owner can engage a consultant or freelance/ expertise in accounting** to prepare and manage the company’s accounts.” (R6)*

Furthermore, external consultants bring a breadth of experience and industry knowledge that may not be readily available within the SME. These experts can offer valuable insights, best practices, and innovative solutions tailored to the specific needs and challenges of the business. Moreover, by engaging external professionals, SME owners can free up their own time and resources to focus on core business activities, such as product development, marketing, and customer service, potentially leading to improved overall performance and competitiveness.

On the other hand, proponents of developing in-house financial expertise argue that relying too heavily on external consultants can lead to a dependency syndrome, where SME owners become overly reliant on external parties for critical financial functions. Moreover, for SMEs operating within complex institutional networks, outsourcing tasks to professionals and consultants may potentially lead to a shift from institutional to personal relationships in addition to a sense of dependency on external resources (Bellini & Fortunato, 2019). This reliance may pose risks in terms of confidentiality, continuity, and control over financial information and decision-making processes. Additionally, outsourcing financial tasks can be costly, particularly for cash-strapped SMEs operating on tight budgets.

4.4. Impact on Financial Sustainability

All respondents concurred with the statement that financial literacy among SME owners is a crucial factor in ensuring effective business management. Firstly, financial literacy significantly influences the financial management of businesses. SME owners must possess a solid understanding of financial concepts and tools to effectively manage their company's finances. Without adequate financial literacy, SME owners may struggle to make informed decisions, leading to financial instability and potential business failure. Research has shown that businesses with higher levels of financial literacy tend to exhibit better financial management practices, resulting in improved performance and profitability.

The lack of sufficient financial literacy can lead to making inaccurate financial decisions. SME owners who lack the necessary financial knowledge may misinterpret information or overlook critical indicators, resulting in suboptimal decision-making. This can have detrimental effects on the financial health of the business, leading to cash flow problems, excessive debt, and missed growth opportunities. Therefore, enhancing financial literacy among SME owners is essential to mitigate these risks and improve overall financial management effectiveness.

“Incomplete information or a lack of awareness of significant aspects pertaining to finances can, indeed, result in bad decision-making, which in turn can have a negative impact on the organisation.”(R1)

Adequate financial literacy is a significant factor in accessing funding from government agencies and financial institutions. Lenders and investors often assess the financial acumen of SME owners when evaluating loan applications or investment proposals. SME owners with higher levels of financial literacy are better equipped to prepare accurate financial statements, develop realistic financial projections, and communicate effectively with potential financiers. As a result, they are more likely to secure funding to support business growth and expansion.

Lastly, the degree of financial literacy significantly influences the long-term sustainability of SMEs. Businesses operating in dynamic and competitive environments must adapt to changing market conditions and make strategic financial decisions to remain viable. SME owners with strong financial literacy skills are better equipped to navigate economic challenges, identify growth opportunities, and implement effective financial strategies. In contrast, businesses with inadequate financial literacy may struggle to survive in competitive markets and may be more susceptible to crises or market disruptions.

“To grow and extend the business, the answer is yes. One of my goals is to establish a training centre, for instance. For this reason, I need to take into account a great deal of information pertaining to money, such as budgeting, costing, and sales forecasting, in order to decide whether the investment is viable.”(R6)

4.5. Government/Zakat Assistance

The question of whether governmental assistance is sufficient to guarantee the growth and sustainability of SMEs is a complex and multifaceted issue. In analysing respondents' responses, which varied in their perspectives, we can explore the strengths and weaknesses of government assistance and support programmes for

SMEs in Malaysia.

Most respondents agreed with the adequacy of government assistance; this may indicate overall satisfaction with the support provided. They have benefitted from various government initiatives, such as financial grants, tax incentives, training programmes, and access to markets. These respondents likely perceive the government's efforts as effective in fostering SME growth and sustainability, contributing positively to their business operations and development. In recent times, the Government of Malaysia has allocated a total of RM44 billion in the 2024 Budget for loan facilities and financing guarantees benefiting Malaysian SMEs (Hamid, 2023).

However, a dissenting opinion from one respondent who expressed dissatisfaction with the government's support suggests that there may be some gaps in the assistance initiatives. This respondent encountered difficulties due to inadequate oversight and monitoring by government agencies, which could have ensured the company's long-term sustainability (R7). Another respondent highlighted the abundance of government opportunities and assistance during the COVID-19 pandemic, reflecting a positive outlook on the government's response to crises. It suggests that government intervention during challenging times can be instrumental in supporting SMEs and mitigating the impact of economic shocks (R3). This perspective underscores the significance of responsive and adaptable government policies to address emerging challenges and crises faced by SMEs.

On the other hand, another respondent mentioned the government's neglect of certain sectors, such as the construction industry, raising concerns about the equitable distribution of support. It suggests that some SME industries may receive inadequate attention from the government, leading to disparities in support and opportunities for growth. This highlights the importance of ensuring that government assistance programmes are inclusive and address the needs of all SMEs, regardless of their sector or size.

In conclusion, while the majority of respondents perceive government support for SMEs as adequate, dissenting opinions and concerns about sectoral neglect highlight areas for improvement. To ensure the growth and sustainability of SMEs, governments must adopt a holistic approach that addresses the diverse needs of SMEs, provides targeted assistance during crises, and promotes inclusivity and equity in resource allocation. For effective programme execution, good coordination between the central government, state governments, and other relevant authorities is crucial. It is important to monitor the efficacy of government

assistance and support programmes for SMEs to ensure accountability and facilitate ongoing development. Continuous dialogue between policymakers and SME stakeholders is also essential to refine and enhance government support programmes and foster a conducive environment for SME development.

4.6. Zakat Assistance: Bridging Financial Literacy and SME Sustainability

The findings revealed that five participants demonstrated a lack of awareness regarding zakat assistance. One participant's understanding suggested that zakat is primarily associated with the *asnaf* category, implying that assistance is reserved for those meeting specific criteria. Additionally, this respondent expressed uncertainty about whether zakat authorities extend assistance to businesses (R6).

Moreover, discussions regarding zakat assistance to *asnaf* entrepreneurs are often associated with various issues, including insufficient capital assistance, the absence of additional aid, or the Al-Qard borrowing scheme to help *asnaf* entrepreneurs develop their businesses. Conversations regarding the formulation of policies concerning the allocation of zakat to the *asnaf* demographic may consider the prevailing needs or primary concerns of the Islamic society during that period. For example, the eligibility criteria for the *asnaf* group should be re-evaluated. The determination of eligibility for the *asnaf* group may not only consider the individual sufficiency threshold (haddul kifayah) of SME business owners but also involve an assessment of business performance.

“Revise the terms of asnaf, both for individual and business entrepreneurship. Consequently, there is a greater potential for facilitating assistance to Muslim SMEs. Furthermore, zakat authorities should actively promote their help on a large scale.”(R7)

Furthermore, collaboration between the government and zakat institutions is crucial to ensure that assistance provided to SME entrepreneurs is complementary. With various forms of financial capital and loans provided by the government, zakat institutions should consider new mechanisms for frameworks to assist entrepreneurs in addressing critical issues, such as sustaining the financial position of Muslim SMEs due to a lack of knowledge and skills in financial literacy.

“To complement what the government does not offer and with the intention of assisting Muslim SMEs to sustain their business.”(R6)

Finally, most respondents agreed that efficiently and effectively distributed zakat assistance could enhance financial literacy and strengthen the financial position of their companies. Only one respondent disagreed with this view (R6). However, to

ensure effective distribution of zakat to entrepreneurs, financial assistance alone is insufficient without being supported by monitoring and evaluation, especially regarding operational and financial management processes (R4).

After a thorough examination of the study’s findings, this study proposes a model for distributing zakat funds to the community of *asnaf* entrepreneurs in the form of non-cash assistance by providing expertise services in various key areas of financial management, such as financial consulting, auditing, and taxation, to enhance the financial literacy of Muslim SME entrepreneurs. This will additionally aid them in enhancing their business performance with greater efficacy and sustainability (Diagram 2).

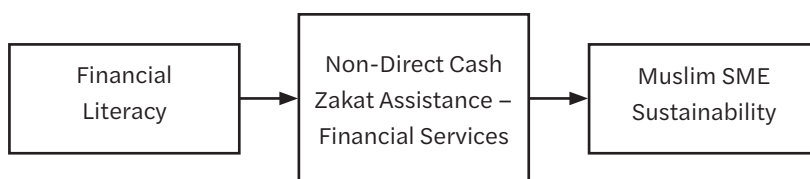


Figure 2. Model of Non-Cash Zakat Distribution for Financial Management Services

This model is proposed after thoroughly examining the key findings of the study. Zakat assistance should focus on the capabilities and competencies of SME entrepreneurs in terms of financial literacy, considering that financial literacy issues are not only a significant problem at the national level but are also a major concern for SMEs globally (Harpal, 2023). The proposed model is in the form of non-cash assistance because cash assistance and training programmes are the main existing types of assistance provided by zakat institutions and the government. The suggestion to provide non-cash assistance aims to ensure the effectiveness of SMEs and opportunities to enter bigger size markets, aligning with the study by (Shiyuti *et al.*, (2022). This is further supported by the research findings and the suggestions of R6 and R7, who stated that focusing on a support system can have a positive impact on entrepreneurs compared to existing financial capital and training programmes. Finally, this framework is formulated by considering the consensus among the majority of participants in the study. They asserted that financial literacy significantly influences the financial management performance of SME entrepreneurs. These outcomes are also in line with research conducted by Grana-Alvarez *et al.* (2022).

A study conducted in Indonesia on non-cash zakat distribution revealed how zakat can be transformed into a tool for long-term SME sustainability, especially

under economic strains like those imposed by the COVID-19 pandemic. In this context, Hakimi *et al.*, (2024) examined a productive zakat model that shifted from traditional cash aid toward non-cash, capacity-building assistance to foster sustainable income and reduce poverty. The study was conducted with the involvement of two zakat institutions (LAZIS Muhammadiyah and Inisiatif Zakat Indonesia), both of which support SMEs through targeted empowerment programmes. This model employs a dual approach to ZIS (zakat, infak, sedekah) fund distribution, incorporating both a top-down strategy, where zakat institutions select SMEs with high growth potential and a bottom-up approach, which allows SMEs to request specific assistance according to their needs. The model's framework includes three key components: business development training, which enhances entrepreneurial and management skills; spiritual and ethical guidance to align business practices with Islamic values; and financial planning, which strengthens financial literacy and resource management. Together, these elements aim to build resilience and sustainability in the SME sector, empowering business owners to contribute to economic recovery and growth. The findings by Hakimi *et al.* (2024) underscore the model's effectiveness, revealing a 53% income increase among SMEs receiving productive ZIS support, which enabled them to maintain stability and avoid debt. While skill enhancement was not immediately significant, the model's impact on financial stability demonstrates its potential to help SMEs develop resilience in times of crisis. This productive zakat approach aligns with broader global trends in financial empowerment, emphasising the role of zakat as a tool not only for immediate relief but also for sustainable economic inclusion and poverty alleviation.

The research by Hakimi *et al.* (2024) complements the findings of (Widiastuti *et al.*, (2021), who validated the effectiveness of a non-cash, productive zakat distribution model that emphasises financial literacy and business development as mechanisms for enhancing SME welfare and reducing dependence on zakat aid. This model's non-cash approach fosters sustainable growth through skill-building and capacity development among zakat recipients. However, the challenges inherent in existing zakat programmes present significant obstacles that could hinder the effective implementation of the proposed non-cash zakat distribution model. As noted by Zuhairah *et al.* (2023), a primary challenge arises from the behavioural tendencies of *asnaf*, who often exhibit reluctance to actively engage in opportunities for self-improvement. This over-reliance on zakat assistance fosters a dependency mindset, undermining the effectiveness of initiatives aimed at

promoting self-sufficiency and sustainable empowerment. Furthermore, Zuhairah *et al.* (2023) highlighted that zakat institutions frequently face difficulties in designing and implementing programmes capable of addressing the diverse and evolving needs of *asnaf*. Although many of these programmes are well-structured, the absence of robust and continuous monitoring mechanisms poses a significant limitation. Ongoing oversight is critical to ensuring that recipients under the productive zakat model achieve sustainable success in their business ventures. To ensure the effective implementation of the non-cash model, these challenges must be addressed through the establishment of structured monitoring frameworks, continuous capacity-building efforts, and targeted strategies to reduce dependency among *asnaf* (Zuhairah *et al.*, 2023). Moreover, collaboration with government agencies and subject-matter experts is indispensable for designing adaptive and comprehensive programmes that meet the evolving needs of *asnaf*. Such collaborative efforts can enhance the model's capacity to empower *asnaf* and support sustainable economic growth within the Muslim SME sector.

Expanding on this framework, this study advances a more specialised form of non-cash support, incorporating expert services in areas such as financial and business consulting to elevate the financial literacy and management competencies of Muslim SME entrepreneurs. Collectively, these studies underscore that a zakat model grounded in skill-based training and specialised financial expertise represents a highly effective mechanism for sustainable economic empowerment and poverty alleviation, positioning zakat as a critical driver of SME resilience and long-term viability. Diverging from traditional, predominantly cash-based zakat models that offer only temporary relief, this study proposes a distinct approach centred on non-cash assistance. By integrating expert services in financial and business consulting, this model directly equips Muslim SME entrepreneurs with essential financial acumen and management competencies, fostering a self-sustaining cycle of empowerment and advancing financial independence.

The implications of this study for policymakers and practitioners are significant, as they shed light on critical issues related to financial literacy among SME owners. Tackling these issues is essential, given that financial literacy can significantly improve the financial management practices of Muslim entrepreneurs. This, in turn, plays a pivotal role in lifting the *asnaf* community out of poverty and fostering broader economic advancement within the country. Policymakers should thoroughly review the results of this study. It is important to highlight that all participants who had not previously received zakat assistance were unaware of available business

aid programmes from zakat institutions. Therefore, a review of the determination of the categories of *asnaf* for assistance schemes involving entrepreneurs and SMEs should be undertaken to ensure that aid is distributed more widely and effectively. Thus, policymakers should consider integrating strategies aimed at promoting financial literacy and expanding support programmes tailored to the needs of Muslim SMEs and entrepreneurs, particularly those belonging to *asnaf* communities. By doing so, policymakers can foster an environment conducive to economic empowerment and sustainable development, ultimately contributing to the prosperity and well-being of the Muslim community.

5. Conclusion

This study highlights the significant financial literacy challenges faced by SME owners in Malaysia, particularly Muslim entrepreneurs, leading to poor financial management and performance. The research demonstrates the potential role of zakat as a mechanism for addressing these issues by offering targeted assistance to Muslim SME entrepreneurs. Insights gathered from semi-structured interviews with seven Muslim SME owners reveal how zakat can enhance financial literacy and promote sound financial management practices. The study proposes a Model of Non-Cash Zakat Distribution for Financial Management Services, aimed at providing non-cash financial management expertise to *asnaf* SME owners. The implications of these findings extend to policymakers, financial institutions, and zakat administrators, suggesting that by effectively utilising zakat funds, they can support Muslim SMEs and contribute to grassroots economic development. This research adds to the ongoing discussion on the intersection of Islamic finance principles and SME development, offering practical insights for stakeholders.

This study's main limitation is that it does not explore the potential role of digital technologies in enhancing the financial literacy of SME owners. Additionally, it does not examine financial attitudes specific to Muslim SMEs, redefine the concept of *asnaf* for business assistance, or address the competency of SME owners—key factors that are essential for ensuring effective and efficient financial management within businesses. Therefore, future research can examine these areas.

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