

Impact of Digital Capability on SMEs Performance: Mediating Role of Digital Business Transformation

Dwiputra Hutama^{1*}, Kusdi Raharjo², Agung Nugroho³

¹Master of Business Administration, Faculty of Administration Sciences, University of Brawijaya, Malang, Indonesia *

²Department of Business Administration, Faculty of Administration Sciences, University of Brawijaya, Malang, Indonesia

³Department of Business Administration, Faculty of Administration Sciences, University of Brawijaya, Malang, Indonesia

Abstract

This study aims to examine and analyze the effect of Digital Capability on Business Performance through the mediation of Digital Business Transformation. This study seeks to determine the business performance of an SME by evaluating digital business capabilities and transformation owned by SMEs in the Greater Malang area. This type of research is explanatory research with a sample of 330 UKM in the Greater Malang area, especially in the culinary, craft, and fashion fields. The sampling technique used in this study is the quota sampling technique, and the analysis method uses Structural Equation Modeling (SEM) analysis with the SmartPLS approach. The findings in this show that Digital Capability significantly influences Business Performance directly and simultaneously through the mediation of Digital Business Transformation. The limitations in this study are the existence of obstacles to access for SMEs in the Greater Malang area, which incidentally has a very large area, so it takes quite a long time, coupled with the Covid-19 pandemic that has hit Indonesia, access is constrained due to the government's social distancing policy.

Keywords: SME, digital, capability, transformation, performance

INTRODUCTION

In the current digital era, businesses, including micro, small, and medium enterprises (MSMEs), are required to have digital literacy and capabilities to develop their ventures. This condition has become a crucial part of the Industry 4.0 era, which is based on the Internet of Things (IoT) and big data. Digital literacy and capabilities in the world of trade continue to evolve in the Industry 4.0 era, regardless of the presence or absence of the COVID-19 pandemic. The pandemic has proven that MSMEs are productive and consistent businesses that can support Indonesia's economic growth at both macro and micro levels [1]. Therefore, MSMEs need to continuously adapt to the development of the digital world to strengthen their contribution to Indonesia's economic growth. With the advancement of information technology, such as social media, business activities can be conducted both offline and online. Through online platforms, businesses can gain more visibility, which greatly assists their growth process. Prioritizing digital literacy and

capabilities among MSMEs is crucial to ensuring their continued significant role [1].

The Ministry of Communication and Information Technology (Kominfo) acknowledges the existing gap between the demands of digital literacy and capabilities in the digital technology era and the current level of digital literacy among Indonesian society, including MSMEs. This gap is attributed to unequal access to the internet. However, during the pandemic, the information and communication sector was the only sector that showed positive double-digit growth [2]. Based on the data, Indonesia's digital literacy index, as surveyed in 34 provinces, has not yet reached a "good" score (4.00), indicating that the national digital literacy index is still at a "moderate" level [2].

The National Information and Communication Technology Council (Wantiknas) also states that the future economy will rely on the nation's ability to innovate. The nation's innovation capacity is closely related to literacy, knowledge, skills, and the ability to engage in entrepreneurship through conventional, digital, and technological literacies [3]. Therefore, MSME entrepreneurs must continually enhance their digital literacy, along with their conventional and technological literacies, to remain competitive in the Industry 4.0 era.

Considering the significant role of MSMEs in national economic growth, the sustainability of

Correspondence address:

Dwiputra Hutama

Email : hutama0203@gmail.com

Address : Faculty of Administration Science, Jl. MT.Haryono
163 Malang 65145, Indonesia

these businesses becomes crucial to explore further. Maximizing available resources is an essential component of MSME sustainability. According to Hai [4], in the current digital era, there are three primary resources that positively impact the digital transformation of MSMEs: the utilization of information technology, digitally capable human resources, and effective business strategies. To enhance competitiveness, MSMEs must build their reputation and intangible assets. The quality of resources, particularly in information technology and human resources, is crucial for each individual MSME due to their heterogeneous and immobile nature [5]. Heterogeneity refers to the different capabilities and levels of ICT literacy among each MSME, while immobility implies that the quality of human resources is not easily replicated from one company (MSME) to another in a short period of time.

MSME entrepreneurs must enhance their digital capabilities, such as utilizing various social media platforms to market their products and services online. This approach allows them to capitalize on the fact that in Indonesia, 48% of internet users search for products and services online, 46% visit online stores, 34% conduct transactions via computers or laptops, and 33% conduct transactions via mobile phones [1].

Society has become more closely connected to the use of technology in digital financial products and services. This can be seen in the increased transactions in mobile banking, e-wallet top-ups, and e-commerce. According to the Indonesian Central Bank (BI), the number of users of the Quick Response Code Indonesian Standard (QRIS) has reached 13.4 million, with 95% of users being MSMEs [6]. This situation predicts that MSMEs and businesses that fail to transform using digital technology are likely to fall behind [7].

In general, the above conditions indicate a relationship between information technology literacy and digital capabilities and digital transformation. The future trend of digital technology adoption will greatly depend on the empirical experience of business owners. If it is proven to significantly improve business performance, its usage will expand throughout the country, especially in areas with adequate internet infrastructure.

Within the province of East Java, overall financial literacy is above the national average. In 2019, based on data from the Financial Services Authority (OJK), the financial literacy rate in East Java reached 88%, and when combined with

students and MSMEs, it reached 92%. The role of MSMEs in the regional economy is also significant. Based on data from the East Java Cooperative and MSME Agency (K-UMKM), the contribution of K-UMKM to the regional economy since 2016 is around 56%. Despite a decrease in 2020 during the pandemic, the contribution of K-UMKM to East Java's Gross Regional Domestic Product (PDRB) still reached 57.25%, which is lower than 2019 but higher than 2018.

In terms of digital transformation, several developments have taken place in East Java, including training and mentoring for micro-businesses in Tuban by Bank Jatim and LinkAja, the dissemination of QRIS usage for MSMEs in the Kediri residency by Bank Indonesia (BI), the utilization of QRIS in Kampung Inggris, Pare, Kediri, which has transformed the village into a digital village, and the "Non-Cash Movement, Smart Digital Payment Solutions" campaign to promote digitalization among MSMEs in Surabaya. The Jatim Kominfo Festival (JFK) 2022, with the theme "Optimistic East Java Rises with Digital Transformation," targets the MSME sector to utilize digital platforms more effectively. Specifically for East Java, Bank Indonesia aims for 1.5 million merchants to use QRIS.

In the city context, the digital transformation of MSMEs in Malang is worth noting. As the second-largest city in East Java, Malang has a significant number of MSMEs. However, the level of digital literacy and digital capabilities among MSME players still needs improvement. Efforts have been made to enhance digital literacy and capabilities among MSMEs in Malang, both before and during the pandemic. Concrete steps include the formation of the Greater Malang area House of Change (RPMR) community, which actively participates in workshops organized by the Malang City Economic Department in collaboration with OJK to make MSMEs more digitally savvy. The Malang City Government also provides opportunities for creative economy actors through the establishment of the Malang Creative Centre (MCC) to support the growth of digital companies.

The reasons why digital literacy and capabilities among MSME players in Malang are continually being enhanced include the following: 1) MSMEs in Malang have demonstrated considerable resilience. Despite the pandemic, e-commerce MSMEs in Malang managed to grow by 123%. Moving forward, it is expected that MSMEs will remain a sector capable of controlling inflation and continue to thrive, especially since

they have already expanded into the digital commercial world. 2) The contributions of K-UMKM to the local economy in the Greater Malang area are as follows: 56.36% in the City of Malang, 67.34% in Malang Regency, and 58.63% in Batu City (see Figure 1.2). The contribution of K-UMKM players in the City of Malang to their respective PDRBs is relatively lower than that of the other two local governments in the Greater Malang area (Batu City and Malang Regency). Therefore, through the Mayor's Program, the Malang City Government continues to promote opportunities for MSMEs to contribute to the regional economy and community income, especially in the current digital era.

Regarding the role of digital transformation for MSMEs at both the provincial and city levels (Malang), specific scientific publications or research currently need to examine the impact of digital transformation on the performance of MSMEs. Digital literacy and capabilities have indeed developed, supported by various government programs. Similarly, data on the use of digital IT for business continues to show growth.

However, the influence of digital IT usage on the performance of MSMEs in the Greater Malang area has yet to be published, considering that many MSMEs still need to familiarize themselves with using digital IT to enhance their businesses. Therefore, it is important to study the relationship between digital transformation (through literacy and capabilities) and the performance of MSMEs.

In understanding the relationship between resources, capabilities, competitive advantage, and profitability, particularly in maintaining a competitive edge over time, the Resource-Based View (RBV) theory is considered as the primary approach [8]. The RBV theory argues that resources assist companies in analyzing opportunities and neutralizing threats [9]. It states that it is advantageous for a company to pursue strategies not currently employed by its competitors. According to Wheelen and Hunger [10], resources are the assets and foundation of a company.

The digital capability of SMEs is observed in this research to see the dynamic capability of SMEs in achieving and sustaining competitive advantage and carve out a distinct identity within fiercely competitive industries [11][12]. The capability includes: a) the ability to acquire digital technology; b) the ability to identify new digital opportunities; c) the ability to master the latest digital technology; d) The company's ability to

develop innovative products/ services/ processes using digital technology [13]. In this perspective, digital capability is very close to digital literacy.

The next significant quality of resource to observe is digital business transformation. This quality refers to a way for companies to use digital technology to develop new digital business models that help create and customize more value for companies [14]. The indicators of digital business transformation refer to the research written by Lin et al. [15], Yu et al. [16], and Venkatesh et al. [17].

The influences of those qualities are measured toward the business performance, which is defined as a measure of the success of an organization or company in achieving its goals [18]. Three important variables of business performance, among others, are sales rate, net profit rate, and cash flow rate/cash flow [13], [18]. Based on the literature review, the hypothesis model of the research is as follows:

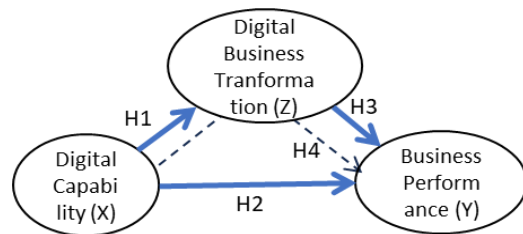


Figure 1. Hypothesis Model of Research Construct

MATERIAL AND METHOD

This research employs a quantitative method and falls into the category of explanatory research, which aims to uncover explanations about the relationships or phenomena that occur among variables, ultimately providing an understanding of cause-and-effect relationships [19].

Data Collection

The data used in this study are primary data collected through questionnaires. The research focuses on 330 SMEs in the culinary, handicraft, and fashion sectors in the Greater Malang region. The sample selection is conducted using a Non-Probability Sampling technique, specifically quota sampling, where the number of selected elements in each sample group is determined based on proportional quotas.

The variables examined in this research consist of independent variables, intervening variables, and dependent variables. The independent variables in this study are Digital Capability (X).

The intervening variable is Digital Business Transformation (Z), and the dependent variable is Business Performance (Y). The measurement scale used is a Likert scale ranging from 1 to 5, indicating respondents' levels of disagreement to agreement.

Data Analysis

Digital Capability (X) has four indicators, while Digital Business Transformation (Z) has three indicators, and Business Performance (Y) has three indicators. Each indicator has several items, as shown in the following table:

Table 1. Indicators and items of each variable

Variables	Indicators & items
Digital Capability (X)	Digital technology (X1) [13]: <ul style="list-style-type: none"> • The use of digital equipment (X1.1) • The use of various software (X1.2)
	New digital opportunity (X2): <ul style="list-style-type: none"> • The use of digital technology data to run business (X2.1) • The use of digital technology data to open new opportunities (X2.2)
	Mastering in digital technology (X3): <ul style="list-style-type: none"> • The use of digital media to support business (X3.1) • The use online marketplace for selling and marketing (X3.2)
	Development of products/services/innovative process (X4): <ul style="list-style-type: none"> • Ability to develop company website (X4.1) • Ability to develop and update website content (X4.2)
Digital Business Transformation (Z)	Technological transition & difusion in business (Z1)[15]: <ul style="list-style-type: none"> • Digitalization for business activity (Z1.1) • Planned digital reformation (Z1.2) • Having clear guidelines in business digitalization (Z1.3) • Updating recent technology development (Z1.4)
	Digital transition for selling (Z2): <ul style="list-style-type: none"> • Adapt digital technology for sales activities (Z2.1) • Modification of selling to adapt to digital changes (Z2.2) • Market segment adjustment due to changes in digital promotion technology (Z2.3) • Product selection for digital marketing (Z2.4)
	Digital technology Usage for business (Z3):

Variables	Indicators & items
Business Performance (Y)	<ul style="list-style-type: none"> • Searching new platform to sell products digitally (Z3.1) • The use of reports from various platforms in business decision-making (Z3.2) • The use of social media to introduce products (Z3.3)
	Selling rate (Y1) [13], [18]: <ul style="list-style-type: none"> • Selling increase in two years
	Profit rate (Y2): <ul style="list-style-type: none"> • Profit increase in two years
	Cashflow rate (Y3): <ul style="list-style-type: none"> • Performance in on-time payment

Sources: [13], [15], [18]

RESULT AND DISCUSSION

The results of the research consist of four: outer model reflective, inner model formative, hypothesis test, and mediation effects.

Outer Model Reflective

Evaluation of the reflective measurement model is a stage that aims to evaluate the construct's validity and reliability.

- Reflective Indicator Loading measures the validity of indicators of the outer loading of each variable. The recommended loading value is above 0.708, but in this research, the loading value of 0.6 is considered sufficient [20]. The result is shown in Table 2.

Table 2. Reflective Indicator Loading Results

	Digital Capability (X)	Digital Business Transformation (Z)	Business Performance (Y)
X.1.1	0,677		
X.1.2	0,776		
X.2.1	0,876		
X.2.2	0,900		
X.3.1	0,846		
X.3.2	0,752		
X.4.1	0,765		
X.4.2	0,800		
Y1			0,918
Y2			0,913
Y3			0,674
Z1.1		0,832	
Z1.2		0,852	
Z1.3		0,860	
Z1.4		0,885	
Z2.1		0,908	
Z2.2		0,900	
Z2.3		0,886	
Z2.4		0,907	
Z3.1		0,797	
Z3.2		0,824	
Z3.3		0,809	

- b. Internal Consistency Reliability: aims to assess the reliability of indicators consistently by looking at the results of Composite Reliability and Cronbach's alpha. The minimum rating for exploratory research is 0.6 [21]. The following table shows the results.

Table 3. Internal Consistency Reliability

	Cronbach's Alpha	Composite Reliability
(Y)	0,783	0,878
(Z)	0,965	0,969
(X)	0,919	0,935

- c. Convergent validity: aims to assess the extent to which constructs converge to explain the variance of the indicators; the metric used to evaluate this is average variance extracted (AVE), with a minimum acceptable value of 0.5 or higher [21].

Table 4. Convergent Validity Results

	Average Variance Extracted (AVE)
(Y)	0,710
(Z)	0,741
(X)	0,643

- d. Discriminant validity: aims to assess the extent to which a construct or variable is truly different from other constructs or variables, with the measurements used, namely the Fornell-Larcker Criterion and the Heterotrait-Monotrait Ratio (HTMT) [21].

Table 5. Fornell-Larcker Criterion and HTMT Results

Fornell-Larcker Criterion Results			
	(Y)	(Z)	(X)
(Y)	0,843		
(Z)	0,499	0,861	
(X)	0,519	0,797	0,802
Heterotrait-Monotrait Ratio (HTMT) Results			
(Y)			
(Z)	0,576		
(X)	0,612	0,841	

Based on the results of the Fornell-Larcker Criterion seen in Table 4, the value of each variable or construct is greater than the correlation value between constructs and other constructs in the model, so the model is said to have a good value of discriminant validity. As for the results of the Heterotrait-Monotrait Ratio (HTMT) seen in Table 5 show that each variable or construct has a good discriminant validity value because each variable or construct has a value of less than 0.9.

Inner Model

Testing the structural model (Inner Model) aims to measure and test the relationship between variables in a structural model.

- a. Collinearity: the collinearity results by looking at VIF values below 5, meaning there are no critical collinearity problems from these results.

Table 6. Collinearity Results

	(Y)	(Z)	(X)
(Y)			
(Z)	2,739		
(X)	2,739	1,000	

Based on the results of Table 6 shows that all VIF values are below 5, so there is no multicollinearity problem or there is a strong intercorrelation between the independent variables.

- b. Coefficient of Determination (R2): the value of the coefficient of determination (R2) is expected to be between 0 and 1.

Table 7. Coefficient of Determination (R2) Scores

	R Square
Digital Business Transformation (Z)	0,635
Business Performance (Y)	0,289

Table 7 shows the R-square (R2) value for the Digital Business Transformation (Z) variable obtained at 0.635 which indicates that 63.5% of the Digital Business Transformation (Z) variable can be influenced by the Digital Capability (X) variable, while the remaining is 36. Other variables outside the research influence 5%. The R-square value for the Business Performance (Y) variable is 0.289, which indicates that 28.9% of the Business Performance (Y) variable can be influenced by Digital Capability (X) and Digital Business Transformation (Z) variables, while the remaining is 71.1 % influenced by other variables outside the research.

- c. Effect Size (f2): illustrates the magnitude of the influence of exogenous latent variables on endogenous latent variables in structural arrangements, with the criterion value of f2 each of 0.35 classified as a strong influence, while 0.15 is classified as a moderate influence, and 0.02 is classified as a weak influence.

Table 8. Effect Size (f2) Results

	(Y)	(Z)	(X)
(Y)			
(Z)	0,028		
(X)	0,057	1,739	

Based on the results from Table 8, it can be concluded as follows:

- The criteria for the Effect Size (f2) value as a strong influence (0.35 or more), namely - The variable Digital Capability (X) to Digital Business Transformation (Z) has a value of 1.739.
- The criteria for the effect size (f2) as a weak influence (0.02 to 0.14), namely:
 - Variable Digital Capability (X) to Business Performance (Y) has a value of 0.057
 - Variable Digital Business Transformation (Z) to Business Performance (Y) has a value of 0.028.

The result of the significant effect size (f2), which is different from the results of the significant path coefficient, indicates that there is partial mediation [22].

d. Predictive Relevance (Q2): the test was conducted to show how well the observed values were generated, with the guideline that if the Q2 value is greater than 0 (Q2 > 0) it illustrates that the model has good predictive relevance.

Table 9. Predictive Relevance (Q²) Scores

	SSO	SSE	Q ²
(Z)	3630,000	1936,838	0,466
(X)	990,000	797,249	0,195

Based on Table 9, which table is calculated from the SmartPLS application, the Q2 results for all variables in the table have a value of more than 0, which indicates that all variables have good predictive relevance results.

e. Path Coefficients: if the path coefficients value is in the range 0 to 1, then it can be declared positive, whereas if the value is in the range -1 to 0, then it can be stated negative

Table 10. Path Coefficients Results

	(Z)	(Y)
Digital Capability (X)	0,797	0,333
Digital Business Transformation (Z)		0,234

Based on the results from Table 10, it can be concluded as follows:

- 1) The direct effect of Digital Capability (X) on Digital Business Transformation (Z) is 0.797, which means that if X1 increases by one unit, Z can increase by 79.7%. This influence is positive.
- 2) The direct effect of Digital Capability (X) on Digital Business Transformation (Z) is 0.333, which means that if X increases by one unit,

Y can increase by 33.3%. This influence is positive.

- 3) The direct effect of Digital Business Transformation (Z) on Business Performance (Y) is 0.234, which means that if Y increases by one unit, Z can increase by 23.4%. This influence is positive.

Research Hypothesis Test

In testing the research hypothesis, the test conducted is to see the significance of the influence between constructs and their indicators. The result can be seen in the following table:

Table 11. Research Hypothesis Test Result

	Original Sample	T-Statistics	P-Values
Digital Capability (X) → Digital Business Transformation (Z)	0,797	36,766	0,000
Digital Capability (X) → Business Performance (Y)	0,333	3,470	0,001
Digital Business Transformation (Z) → Business Performance (Y)	0,234	2,475	0,014

Hypothesis testing can be done by comparing t-statistics with t-tables. A t-table can be obtained from a total of 330 respondents with a significance value of 0.05, so a t-table of 1.960 is obtained.

H1: Digital Capability (X) directly and significantly influences Digital Business Transformation (Z).

The value of the Digital Capability variable (X) to Digital Business Transformation (Z) with a path coefficient of 0.797 and has a t-statistical value of 36.766 which indicates that the t-count is greater than the t-table (1.960), and a p-value of 0.000 ≤ 0.05. The results above show that H0 is rejected and H1 is accepted, so Digital Capability (X1) directly and significantly influences Digital Business Transformation (Z). This means that the first hypothesis (1) is accepted.

H2: Digital Capability (X) directly and significantly positively affects Business Performance (Y).

The value of the Digital Capability variable (X) on Business Performance (Y) with a path coefficient of 0.333 and has a t-statistical value of 3.470 which indicates that the t-count is greater than the t-table (1.960), and has a p-value of 0.001 ≤ 0.05. The results above show that H0 is rejected and H2 is accepted, so Digital Capability (X1) has a direct and significant positive influence on

Business Performance (Y). This means that the second hypothesis (2) is accepted.

H3: Digital Business Transformation (Z) directly and significantly positively affects Business Performance (Y).

The value of the Digital Business Transformation (Z) variable on Business Performance (Y) with a path coefficient of 0.234 and has a t-statistical value of 2.475 which indicates that t-count is greater than t-table (1.960), and has a p-value of $0.014 \leq 0.05$. The results above show that H0 is rejected and H3 is accepted, so Digital Business Transformation (Z) has a direct and significant positive effect on Business Performance (Y). This means the third hypothesis (3) is accepted.

Mediation Effects

The mediating effect of the results of this study is the influence of the research hypothesis indirectly, can be seen in the table below:

Table 12. Mediation Effects Results

	Original Sample	T-Statistics	P-Values
Digital Capability (X) → Digital Business Transformation (Z) → Business Performance (Y)	0,186	2,438	0,015

Based on **Table 12**, there are research findings regarding the indirect effect as follows:

H4: Digital Capability Influences Business Performance through Digital Business Transformation

The effect of Digital Capability (X) through Digital Business Transformation (Z) on Business Performance (Y) obtained a path coefficient value of 0.186, a t-statistic value of 2.438 and a P-value of 0.015. Because the P-value ≤ 0.05 , and the coefficient is positive indicating that there is a significant and positive influence between Digital Capability (X) on Digital Business Transformation (Z) through Business Performance (Y). Thus, the four (4) hypothesis of this study is accepted. The mediation of the hypothesis is partial because Digital Capability (X1) on Business Performance (Y) is significant. However, the coefficient of direct influence (Digital Capability (X) on Business Performance (Y) (0.333)) is greater than the indirect effect (Digital Capability (X) on Business Performance (Y) through Digital Business Transformation (Z) of 0.186), it can be concluded that the real influence is direct.

Discussion

1) Digital Capability to Digital Business Transformation

The results show that Digital Capability significantly affects Digital Business Transformation. This means that Digital Capability is represented by 4 (four) indicators, namely ICT Proficiency, Digital Opportunities, Data and Media Literacy, and Digital Creations, which positively and significantly influence Digital Business Transformation. In other words, the higher the level of digital capability, the higher the tendency for digital business transformation. This is in line with the research by Rupeika-Apoga et al. [23], [24], which states that Digital Capability has a positive and significant effect on Digital Business Transformation. Increasing digital capabilities is carried out through innovation, starting from digital product development to collaboration with various parties using a digital business ecosystem approach so that a business can transform digitally. With digital business transformation, business people can get a new perspective on managing a company, optimizing company operations, and changing business models to be more efficient [25].

2) Digital Capability on Business Performance

The results show that Digital Capability has a significant effect on Business Performance. This can be interpreted that Digital Capability is represented by 3 (three) indicators, namely ICT Proficiency (ICT Proficiency), Data and Media Literacy (Data and Media Literacy), and Digital Creation (Digital Creation), have a significant direct influence on Business Performance. In other words, the higher the level of digital capability, the higher the ability or business performance of an SME. This is in line with Khin & Ho's [13] research which states that Digital Capability positively affects Business Performance both financially and non-financially. The same thing was also stated by Zhe & Hamid [26], stating that a strong positive relationship was found between Digital Capability and Business Performance. Digital capability is basically the ability of a company with its digital technology to manage information internally and externally so that it can become a resource that can bring economic benefits to the company. This is in accordance with the theory of Resource Based View from Barney [8], which states that information technology is a

company resource that can be used to increase competitive advantage for companies.

3) Digital Business Transformation on Business Performance

The results show that Digital Business Transformation has a significant effect on Business Performance. This means that Digital Business Transformation is represented by 3 (three) indicators, namely Diffusion and Transition of Technology in Business, Digital Transition of the Sales Function, and Utilization of Digital Technology, which significantly directly influences Business Performance. In other words, the higher the digital business transformation, the higher the ability or business performance of an SME. This is in line with the research by Teng et al. [27] stated that Digital Business Transformation can impact Business Performance. The same thing was also stated by Avirutha [28], stating that Digital Business Transformation has a positive and significant influence on Business Performance. Digital transformation can be defined as the use of digital technology in various aspects of modern society that go far beyond digital literacy and competence; this is related to the ability of companies to successfully implement new technologies and procedures to improve their business operations [29].

4) Digital Capability on Business Performance through Digital Business Transformation Mediation

The results of the study show that Digital Capability can affect Business Performance both directly and indirectly through Digital Business Transformation. Therefore, Digital Business Transformation mediation can be categorized as a partial mediation. Empirically, this study's results align with the research of Khin & Ho [13], which states that Digital Capability has a positive effect on Business Performance through Digital Innovation. Digital Innovation is also part of Digital Business Transformation because solving digital innovations will make it possible to transform an industry or MSMEs to an optimal level and further accelerate the journey towards a digital economy [13]. However, the direct effect (Digital Capability (X) on Business Performance (Y)) is greater than the indirect effect (Digital Capability (X) on Business Performance (Y) through Digital Business Transformation (Z)), so it can be concluded

that the influence is actually direct. Thus, Business Performance can be improved by developing Digital Capability.

CONCLUSION

The research found that:

1. Digital Capability is able to directly encourage increased Digital Business Transformation for SMEs throughout the Greater Malang area. Qualified digital capabilities can make it easier for SME businesses to transform into digital platforms so that a business becomes more efficient and effective, and the performance of a business can increase.
2. Digital Capability improves Business Performance directly. Qualified digital capabilities can make it easier for SME business people to operate a business so that a business becomes more efficient and effective, and the performance of a business can increase.
3. Digital Business Transformation is able to encourage the direct improvement of Business Performance for SMEs throughout the Greater Malang area. The better the digital business transformation, the better the business performance of SMEs throughout the Greater Malang area.
4. Digital business transformation positively and significantly mediate between digital capabilities and business performance. However, the direct effect (Digital Capability (X) on Business Performance (Y)) is greater than the indirect effect (Digital Capability (X) on Business Performance (Y) through Digital Business Transformation (Z)), so it can be concluded that the influence is direct.

REFERENCES

- [1]. L. Destianah, "Capability in Utilizing Social Media as a Promotion Strategy for Increasing the UMKM Economy," J. CIC Lemb. Ris. dan Konsult. Sos., vol. 3, no. 1, hal. 17–26, 2021, doi: <https://doi.org/10.51486/jbo.v3i1.17>
- [2]. kominfo.go.id, "Hasil Survei Indeks Literasi Digital Nasional 2020, Akses Internet Makin Terjangkau," Kementerian Komunikasi dan Informatika, 2020. https://kominfo.go.id/content/detail/30928/siaran-pers-no-149hmkominfo112020-tentang-hasil-survei-indeks-literasi-digital-nasional-2020-akses-internet-makin-terjangkau/0/siaran_pers.
- [3]. Wantiknas.go.id, "Mengangkat Literasi Digital Masyarakat (Improving community's

- digital literacies),” Dewan Teknologi Informasi dan Komunikasi Nasional, 2020. <http://www.wantiknas.go.id/id/berita/men-gangkat-literasi-digital-masyarakat>.
- [4]. N. T. Hai, “Digital transformation barriers for small and medium enterprises in Vietnam today,” *Laplace Em Rev.*, vol. 7, no. 3A, hal. 416–426, 2021, doi: 10.24115/s2446-6220202173a1424p.416-426
- [5]. M. Sridharan, “RBV – What is a resource-based view of strategy?” *Think Insights*, 2017. <https://thinkinsights.net/strategy/rbv-strategy/> (accessed on Jul 18, 2017)
- [6]. T. Santia, “Pengguna QRIS Capai 13,4 Juta, Didominasi UMKM,” *merdeka.com*, 2021. <https://www.merdeka.com/uang/pengguna-qris-capai-134-juta-didominasi-umkm.html>.
- [7]. I. Safutra, “Sejak Pandemi Covid-19, Bisnis Digital Makin Bergairah (Digital business is flourishing since the Covid-19 Pandemic),” *Jawa Pos*, 2021. <https://www.jawapos.com/ekonomi/bisnis/19/01/2021/sejak-pandemi-covid-19-bisnis-digital-makin-bergairah/> (accessed on Okt 15, 2021).
- [8]. J. Barney, “Firm Resources and Sustained Competitive Advantage,” *J. Manage.*, vol. 17, no. 1, hal. 99–120, Mar 1991, doi: 10.1177/014920639101700108
- [9]. R. F. David dan R. F. David, *Strategic Management Concepts and Cases*. London, UK: Pearson Education Limited, 2015.
- [10]. T. L. Wheelen dan J. D. Hunger, *Strategic Management and Business Strategy*. Hoboken, New Jersey, United States: Pearson Prentice Hall, 2006.
- [11]. H. Bhasin, “What are Dynamic Capabilities and their Role in Strategy?,” *Marketing91*, 2018. <https://www.marketing91.com/dynamic-capabilities/>.
- [12]. D. Teece, *Dynamic Capabilities and Strategic Management: Organizing for Innovation and Growth*. Oxford, UK: Oxford University Press, 2009.
- [13]. S. Khin dan T. C. F. Ho, “Digital Technology, Digital Capability and Organizational Performance: A mediating role of Digital Innovation,” *Int. J. Innov. Sci.*, vol. 11, no. 2, hal. 177–195, 2019, doi: 10.1108/IJIS-08-2018-0083.
- [14]. P. C. Verhoef et al., “Digital transformation: A multidisciplinary reflection and research agenda,” *J. Bus. Res.*, vol. 122, no. July 2018, hal. 889–901, 2021, doi: 10.1016/j.jbusres.2019.09.022.
- [15]. J. Lin, Z. Luo, dan X. Luo, “Understanding the roles of Institutional Pressures and Organizational Innovativeness in Contextualized Transformation toward E-Business: Evidence from Agricultural Firms,” *Int. J. Inf. Manage.*, vol. 51, no. February, hal. 0–1, 2020, doi: 10.1016/j.ijinfomgt.2019.10.010.
- [16]. Y. Yu, M. Li, X. Li, J. L. Zhao, dan D. Zhao, “Effects of Entrepreneurship and IT Fashion on SMEs’ Transformation toward Cloud Service through Mediation of Trust,” *Inf. Manag.*, vol. 55, no. 2, hal. 245–257, 2018, doi: 10.1016/j.im.2017.07.001.
- [17]. V. Venkatesh, M. G. Morris, G. B. Davis, dan F. D. Davis, “User Acceptance of Information Technology: Toward a Unified View,” *Manag. Inf. Syst. Res. Cent.*, vol. 27, no. 3, hal. 425–478, 2003, doi: 10.2307/30036540.
- [18]. R. Purnomo dan S. Lestari, “Pengaruh Kepribadian, Self-Efficacy, dan Locus of Control terhadap persepsi Kinerja Usaha skala Kecil dan Menengah,” *J. Bisnis dan Ekon.*, vol. 17, no. 2, 2010.
- [19]. B. Prasetyo dan L. M. Jannah, *Metode Penelitian Kuantitatif: Teori dan Aplikasi*. Jakarta: PT. Rajagrafindo Persada, 2005.
- [20]. J. F. Hair, G. T. M. Hult, C. M. Ringle, M. Sarstedt, N. P. Danks, dan S. Ray, *Partial Least Squares Structural Equation Modeling (PLS-SEM) Using R*. Berlin, Germany: Springer, 2021.
- [21]. J. F. Hair, G. T. M. Hult, dan C. M. Ringle, “A Primer on Partial Least Squares Structural Equation Modeling (PLS-SEM),” 2017.
- [22]. C. Nitzl, J. L. Roldan, dan G. Cepeda, “Mediation analysis in partial least squares path modelling: Helping researchers discuss more sophisticated models,” *Ind. Manag. Data Syst.*, vol. 116, no. 9, hal. 1849–1864, 2016, doi: 10.1108/IMDS-07-2015-0302.
- [23]. Rupeika-Apoga, Ramona, L. Bule, dan K. Petrovska, “Digital Transformation of Small and Medium Enterprises: Aspects of Public Support,” *J. Risk Finance. Manag.*, vol. 15, no. 45, 2022, doi: <https://doi.org/10.3390/jrfm15020045>.
- [24]. R. Rupeika-Apoga, K. Petrovska, dan L. Bule, “The Effect of Digital Orientation and Digital Capability on Digital Transformation of SMEs during the COVID-19 Pandemic,” *J. Theor. Appl. Electron. Commer. Res.*, vol. 17, no. 2, hal. 669–685, 2022, doi: 10.3390/jtaer17020035.

- [25]. Novita Hifni, "Kapabilitas Digital untuk Kejayaan Global," majalahpajak.net/, 2022. <https://majalahpajak.net/kapabilitas-digital-untuk-kejayaan-global/> (accessed on Sep 13, 2022)
- [26]. B. O. M. Zhe dan N. A. Hamid, "The Impact of Digital Technology, Digital Capability and Digital Innovation on Small Business Performance," Res. Manag. Technol. Bus., vol. 2, no. 1, hal. 499–509, 2021, <http://publisher.uthm.edu.my/periodicals/index.php/rmtb>.
- [27]. X. Teng, Z. Wu, dan F. Yang, "Research on the Relationship between Digital Transformation and Performance of SMEs," Sustainability, vol. 14, no. 6012, hal. 1–17, 2022, doi: 10.3390/su14106012.
- [28]. A. Avirutha, "The Impact of Digital Transformation to Business Performance in Thailand 4.0 Era," Veridian E-Journal, Silpakorn Univ. (Humanities, Soc. Sci. arts), vol. 11, no. 5, hal. 295–307, 2018.
- [29]. D. Cita, W. Purba, M. Muhammad, M. S. Hasibuan, K. Menulis, dan J. Simarmata, Inovasi Pendidikan Lewat Transformasi Digital. Medan: Yayasan Kita Menulis, 2019.