



Impact of Digital Transformation on Small and Medium Enterprises Performance in The Sri Lankan Apparel Sector

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ABSTRACT

The present study aims to determine the impact of digital transformation on the organizational performance of Sri Lankan SMEs in the apparel sector. Digital transformation plays a significant role in many businesses and helps to value the firm's propositions and manage business operations well. Implementing digital platforms is not easier for companies. Small and medium-scale enterprises need to invest more in digital transformations. Digital transformation is more important to apparel sector businesses. Firms must logically acquire new digital technology to become profitable organization, survive, and enhance continuous growth. According to that, the main objective of the study is to determine the impact of digital transformation on organization performance this study adopted the positivist research philosophy, deductive approach and quantitative survey method. The sample of the study consists of 365 Small and Medium Enterprises in the apparel sector located in Western Province, Sri Lanka. Comparability, cost-effectiveness, trust and interactivity are the independent variables and business performance is the dependent variable of the study. The study found that Comparability, cost-effectiveness, trust, and interactivity positively impact business performance. The findings of the study recommend that there should be proper planning and training to make the digital transformation. To address the limitations of the



present study, it suggested for future researchers to conduct the research with more variables and conduct as longitudinal study.

Keywords: *Apparel sector, Complexity, Cost-effectiveness, Digital transformation, Interactivity, SME performance, Sri Lanka, Trust, Western Province*

1. INTRODUCTION

In the 21st century, there is rapid development in information technology, and these changes significantly impact business activities. With that, this research identifies the impact of digital transformation on organizational performance with the compatibility, cost-effectiveness, trust, and interactivity in the SME apparel sector in Sri Lanka. Those four variables verified the SME performance by enhancing the significant role. Considering the impact of digital transformation, the organization needs to upgrade their systems and human capital and introduce programs for the end customers to maximize sales and profit by reducing overhead costs.

Digital transformation is concerned with transforming business processes using technology to implement a new approach to the production process for customer goods and services (Ebert & Duarte, 2018). Digital transformation is associated with new digital technology advances in businesses (Deighton & Kornfeld, 2008). Small and Medium scale enterprises struggle to compete with dynamic environmental changes. Therefore, Small and Medium scale enterprises face competitive pressure and the need to use digital platforms to maintain their business strategies (Cenamor et. al, 2019). Modern technology transformation enhances the effectiveness of communication and helps businesses to sustainable growth (Opoku et. al, 2021).

Especially digital transformations and ICT use in small and medium scale enterprises help to enhance operational efficiency and enhance task management and market operations of the company (Cenamor et. al, 2019). However, implementing digital platforms is not easier for companies since small and medium-scale enterprises must invest more in digital transformations. Therefore, many Small and Medium scale enterprises fail to implement digital transformations (Cenamor et. al, 2019).





Digital transformation in society gives strength to certain businesses, and opportunities, though more small and medium scale enterprises seem as a threat. To manage innovative ideas, small and medium scale enterprises need to follow digital transformations (Koffi et al., 2021). Therefore, the management of small and medium scale enterprises needs to take correct strategies to reach the target market and enhance business profit (Islami, Wahyuni, & Tiara, 2020).

Small and Medium scale enterprises exist for over 75% of Sri Lanka and contribute over 52% to the Sri Lankan economy. But Small and Medium scale enterprises are less successful because of multiple factors. However, the portion of small and medium scale enterprises in Sri Lanka influences the price and quantity of goods in the market though small and medium scale enterprises suffer from certain problems, including limited availability of financial resources, skilled employees, knowledge and ability to manage. Therefore, digital transformations need to reshape business models and strategies. Technology partnership helps change the relationship between workers, customers, employers, and employees. Eliminating barriers helps to help innovative products and implement innovative processes and work together (Rassool & Dissanayaka, 2019)

For digital adaptation, small and medium scale enterprises need to change the existing process of the business. New technology implementation needs to be able to compare the previous method, cost-effectiveness, trust and interaction. To select the best option, small and medium scale enterprises need digital literacy and the ability to handle technical equipment. A survey conducted by the Department of Census and Statistics identified that in Sri Lanka, there is 33.8% digital literacy among the Sri Lanka population. Digital literacy is different from computer literacy. Therefore, this becomes one reason for less adaptation to digital transformations (Gunawardene, 2017).

Less implementation of digital technologies misses the opportunities for organizations such as quick and accurate data collection and record, resource management, providing better customer experience up to customer expected level,



encouraging digital culture for employees and gaining competitive advantages, increasing profit and improving productivity (Pereira et al. 2022). The above indicates the common issues which can face with less digital transformation for business performance.

Compared to other industries, the apparel industry has more new entrances due to the ability to manufacture and export products successfully by utilizing the opportunities in the international and local markets with tailoring designs (Sri Lanka Export Development Board, 2022). This becomes the leading industry which makes employment for more than 350,00 employees (Sri Lanka Export Development Board, 2022). Also apparel industry becomes dynamic and significant contributor to Sri Lanka economy with 6% of GDP contribution in 2022 (Sri Lanka Export Development Board, 2022). It can identify digital disruptions in the apparel industry. The impact of digital disruptions and resistance to digital transformation change has adverse effects on the small and medium apparel sector enterprises (Sri Lanka Export Development Board, 2022). There is less real digital transformation in Sri Lankan apparel industry. These adversely affect businesses to cater to international markets since there are many opportunities to earn more profit. This creates lack of real transparency and visibility of orders and manages the supply chain process. This reduces the ability to control costs and continue business for uncertainty risk (Zachariadis & Ozcan, 2017). Therefore it can identify that in Sri Lanka, Small and Medium scale enterprises in the apparel sector are less adaptable to digital transformation (Gunawardane, 2017).

Researchers emphasized that there is lack of research conducted to investigate the impact of digital transformation in measuring the organization performance of small and medium scale enterprises in Sri Lanka which helps long-term business development (Opoku et. al, 2021). Further, many types of research have been conducted in the context of developed countries than developing countries (Ponis & Lada, 2021). and developing countries promote technologies to survive business, and



as a developing country, Sri Lanka does not have the capabilities to adopt digital transformations with a lack of finances (Adam and Alarifi, 2021).

Based on the above facts, researchers are motivated to investigate "How digital transformations are impacting in measuring organization performance of Small and Medium scale apparel sector enterprises Sri Lanka".

In explicitly, the study is to identify the impact of compatibility, cost effectiveness, trust and Interactivity on the organizational performance of small and medium scale enterprises in Sri Lankan apparel sector. To achieve those objectives, the remainder of the article is organized with sections for literature review, theoretical review, methodology, data analysis, discussion, and conclusion. The literature review section provides insight into the current knowledge level of digital transformation, and the theoretical review discusses the different theories relevant to digital transformation. Under the methodology section, the methods to conduct the research were highlighted. In proceeding, the data analysis section explains the findings of the research whereas the last section, discussion and conclusion, conclude the research by summarizing the entire article by comparing the current research's findings with the literature and providing avenues to future researchers.

2. LITERATURE REVIEW

2.1 Digital Transformation

The term "digital transformation" may be defined in several ways (Vial, 2021). The term "digital transformation" refers to any change brought on by or affected by the pervasive use of digital technologies. Digital transformation, in contrast to the definition offered by Verhoef et al.(2021), is described as the use of technology to enhance the performance or reach of an organization. Another definition says that, digital transformation is the third and greatest degree of digital abilities (Nadkarni & Prügl, 2021). Some of these definitions suggest that digital transformation has far-reaching causes, developments, and repercussions. This facilitates the digital design of information technology and comprehension, assessment, digital value network





design, and feedback from customers for small and medium-sized enterprises (SMEs) (Tabrizi et al., 2019). A data-driven management structure is also required, which calls for the practical use of the Internet across the whole field of design, production, marketing, sales, and presentation (Ebert & Duarte, 2018). This also includes blockchain, simulation, the web, cyber security, and other forms of online safety (Mergel et al., 2019). Additionally, it is helpful to have an open line of communication between business owners and IT professionals to reduce the likelihood of fraud (Fletcher & Griffiths, 2020).

Companies that are compelled to adapt in the face of a pandemic might benefit from expanding their use of digital marketing tools (Kraus et al., 2021). Problems in the distribution and retail channels may therefore be addressed. Small and medium-sized enterprises (SMEs) may help digital transformation succeed by selling their wares on social media, providing discounts, and so on (Gong & Ribiere, 2021). There are four approaches to digital transformation, all aimed at achieving the same goals: (1) keeping the company competitive; (2) boosting productivity inside the company, and enhancing customer experience. Increasing client happiness (3) and simplifying the process of making a variety of strategic choices (4) are goals that may help businesses succeed (Wessel et al., 2021). SME digital transformation requires government and stakeholder cooperation (Ebert & Duarte, 2018). The ultimate goal is for organizations to reach a level of digital maturity that allows them to operate with more efficient and effective business models and procedures (Mergel et al., 2019; Acquila-Natale et al., 2022). These can be broken down into the following categories: company specifics, lack of qualified personnel, lack of knowledge of the required technology, infrastructure, lack of marketing, adoption of ICT, and e-commerce (Kraus et al., 2021), availability of technical road maps and ecologies for digital transformation, and environment dependability (Gong & Ribiere, 2021). Consider, for instance, how the same set of internet apps addresses sales and logistics. Online marketplaces might start to be relied on by the supply chain to link buyers and sellers of raw materials (Reis et al., 2018).

Small and medium-sized enterprises (SMEs) will participate in social media, provided such platforms offer a large quantity of timely, relevant, and high-quality material (Dressler & Paunovic 2021).

2.2 Factors considered by Small and Medium Enterprises for Digital transformation

The business may now be conducted from any location at any time thanks to internet-enabled forms of communication (Schaller, 2018). Several studies that looked at how small and medium-sized enterprises (SMEs) use Facebook found that Facebook was being used for a wide range of organizational purposes, including but not limited to: advertising, interaction, sales, marketing, innovative thinking, resolving problems, customer support, human resource management, information systems, driving culture change (Bughin et al., 2019), and advertising on social networks (Muditomo & Wahyudi, 2020). Henderson, (2020) claim that small and medium-sized enterprises (SMEs) utilize social media platforms like Facebook to facilitate communication and cooperation among employees and with consumers. An international survey of small and medium-sized enterprise (SME) managers found that business innovativeness, age, and geographic location significantly influenced the extent to which SMEs adopted Twitter (Metawa et al., 2021). Dressler & Paunovic, (2021) argue that small and medium-sized enterprises (SMEs) will participate in social media provided such platforms offer a large quantity of timely, relevant, and high-quality material (2011). Compatibility (MAUGERI, 2020), cost-effectiveness (Kuntsman & Arenkov, 2019), trust (Gábor, 2019), and interaction (Berman et al., 1999) are only few of the criteria that have been shown to affect social media adoption. Here, we'll break out the connections between each party.

2.3 Compatibility

According to the Diffusion of Innovations (DOI) hypothesis, an innovation's compatibility is measured by how well it aligns with its prospective adopters Field's values, habits, and requirements (Maugeri, 2020). A key aspect of spreading new

ideas is compatibility (Cooper and Zmud, 1990). If a company knows that a new piece of technology will operate with its existing set of business software, it will be more inclined to consider using that technology. With the ease of material related to a company's goods and services can be created and distributed in the digital age, incorporating digital transformation into business practices is a smart move (Dengler & Matthes, 2018). In light of the lack of consensus, examining how compatibility affects digital transformation is prudent.

Based on the above literature, researchers have developed the following hypothesis.

H₁- There is an impact of compatibility on the performance of small and medium enterprises.

2.4 Cost-Effectiveness

The cost has been shown to have a direct and substantial association with technology adoption and use in previous studies (Kuntsman & Arenkov, 2019). It has been shown that new technology adoption is influenced by how affordable it is (Sandu & Voiku, 2019). As a result of its cheap price, minimal barriers to entry, and low level of IT skills necessary for usage, digital transformation is well-suited for small and medium-sized enterprises (SMEs) (Alshakhshir & Howell, 2021). According to Sandu & Voiku, (2019) when the cost of getting started with new information and communication technologies is high, small and medium-sized enterprises (SMEs) are less likely to embrace such technologies. Alshakhshir & Howell, (2021) found that the adoption cost considerably impacts internet use among Malaysian SMEs. On the other hand, Panel, (2002) found that price didn't matter much regarding people's willingness to use ICT. According to Gluhov & Skiba, (2022) research, the perceived cost does not directly affect ICT adoption. However, businesses may have direct connections with clients at a reasonable cost by using social media.

Based on the above literature, researchers have developed the following hypothesis.

H₂- There is an impact of cost-effectiveness on the performance of small and medium

2.5 Trust

Trust is a complex concept with many facets. The authors of this research analyzed many forms of trust. The institutional trust model is the most appropriate for this investigation. Trust in institutions may be either "situationally normal" or "structurally assured," as defined by (Gábor, 2019). Situational normality is the conviction that one will achieve their goals since doing so is typical in the given circumstance. On the other hand, structural assurances are the confidence that beneficial results are probable due to contextual structures like agreements, rules, and guarantees. Mahmood, (2016) proposed a new category of trust, which they called "informational trust." Informational trust, or a user's conviction in the reliability, trustworthiness, and correctness of Facebook's content, is a major determinant in how often and how much people use the platform (Faruquee et al., 2021). To succeed, small companies need to maintain good relationships with their customers, which may be accomplished via social media. In response to client questions, the company's experts might utilize social media to exchange ideas, views, and information (Kozhevnikov & Korolev, 2018). Small and medium-sized enterprises (SMEs) use Facebook to spread the word about their business, promote their goods and services, and learn new things. Consequently, structural assurance and informational trust may be necessary to utilize Facebook for work-related objectives.

Based on the above literature, researchers have developed the following hypothesis.

H₃- There is an impact of trust on the performance of small and medium enterprises.

2.6 Interactivity

Previous studies have shown that human-technology interaction plays a crucial role in the development of effective information systems (Berman et al., 1999). Among the many aspects of design that affect how people feel about innovative technology, like websites, interactivity stands out as crucial and differentiating (Ksiazek, 2015). Social media platforms like Facebook are examples of interactive media. Unlike

broadcasts or handouts, it enables conversation between sender and receiver (Deighton & Kornfeld, 2008). Based on their research on the usage of Facebook by two Indonesian SMEs, Ebert & Duarte, (2018) concluded that the platform has the potential to serve as a valuable free online marketing tool if handled correctly. Because of this, the interaction construct may have a considerable effect on Facebook use, given the interactive nature of the platform.

Based on the above literature, researchers have developed the following hypothesis.

H₄- There is an impact of interactivity on the performance of small and medium enterprises.

2.7 Performance

Some studies have discussed how technology can affect to process of the business and performance (Paniagua and Sapena, 2014; Hakala and Kohtamäki, 2011). Some studies are demonstrated that they have advantages to the adaptation of social media, and some have discovered the positive relations between social media adaptation and corporate performance. (Paniagua and Sapena, 2014; Rodriguez et al., 2012). Further, Rodriguez et al. (2012) found that social media has improved customer feedback and sales performance. Using social media has developed an organisation's social capital and improved performance (Ferrer et al. 2013). According to Thong, (2001) and Zhu & Weyant, (2003), technology adaptation impacts SMEs' performance, such as financial and non-financial.

3. THEORETICAL REVIEW

Researchers have identified three theories relevant to the present study: organizational learning theory, technology acceptance model and innovation diffusion theory.

Organizational learning theory is focused on creating knowledge and using the knowledge within the organization. The theory emphasises that learning can be done



through interacting with people and helps find solutions for people with new information and changes. Mainly this theory enhances the organizational culture, with knowledge sharing, teaching by failures, encouraging employees and enhancing teamwork. The theory of organizational learning is very much important to digital transformations because it increases employees' knowledge regarding new technical changes, enhances employee job satisfaction, reduces employee turnover, increases company profit, efficiency and productivity, develops leadership qualities and management and enhances quick adaptability for digital changes. According to the organizational learning theory, digital transformation can be done with resource development, enhancing learning culture, changing employees' attitudes, and implementing fast change. This theory is mainly important hence this reduces failures with the new adoption of digital and learning through experience (Bratianu, 2018).

The technology acceptance model can define as how organizations use technology tools for implementation. This theory is important in explaining digital transformation. Organization Digital transformation can be done in several ways. Organizations can newly implement digital technology for organization work, or existing technology processes can be changed to advanced systems. Both can be identified as digital transformation. Mainly this helps to identify users who can accept the technology change. Understanding the model helps to predict better how new information resources can be used. This identification helps to enhance the flexibility of work, confidence in digital transformation and make company control. Finally, it increases knowledge, leading to company productivity (Ma and Liu, 2004).

Innovation diffusion theory was introduced in 1962 by Rogers. This theory mainly explains how, why, and what innovative ideas arise with technological advancement with rapid change in the social system. This theory comes across innovations that arise with new technology changes. This theory encourages people to implement new ideas into practice. The adoption of technology changes can be under five stages. They are Innovators, early adoption, early maturity, late maturity and Laggards. This theory suggests that most organizations implement the technology by considering



relative advantages, comparability, complexity, observation and traceability (Wani and Ali, 2015). Innovation Diffusion theory is supported to identify what factors need to consider and contribute to digital transformation in organizations. Digital transformation is the result of the adoption or implements a technology system with innovative ideas (Steiber et al., 2020).

4. METHODOLOGY

The present study used the positivism philosophy to conduct quantitative research, and the survey method was selected as the research strategy considering research questions, objectives, available time horizon, and the research understanding. This strategy allows for gathering information by asking questions (Saunders & Bezzina, 2015). Further, this study used a cross-sectional time frame with a specific time horizon for conducting the research. A cross-sectional time frame defines what happens in the present moment. This discusses the characteristics of the population in a certain period (Saunders & Bezzina, 2015).

The population of the present study is Small and Medium Enterprises in Sri Lanka. Institute of Chartered Accountants Sri Lanka has specified that there are 30,000 registered Small and Medium Enterprises employed in Sri Lanka, and out of the total Small and Medium Enterprises, approximately there are 25% of businesses currently operate in the Western province of Sri Lanka (ICASL, 2022). Therefore, the research population is 7500 Small and Medium Enterprises in the apparel sector in Western Province, Sri Lanka. The sample size of the population would be 365 of Small and Medium Enterprises in the apparel sector in the Western Province of Sri Lanka. The sample is determined based on the Morgan table, (Morgan, 1970). After determining the sample size, the respondents are selected using random sampling methods to typify the study population in a satisfactory manner. In selecting elements for the sample, researchers have numbered the population from 1 to 7500. Then selected the 20th element in the list and distributed a self-administrated questionnaire to collect data. If the selected element was not available to get a response questionnaire was

given to the 21st element. The study used several research analysis methods to analyze the data to get results that satisfied the three objectives and tested the hypotheses. Descriptive statistics, correlation analysis and Regression analysis are used for determine the impact of independent variables on dependent variables.

5. DATA ANALYSIS

The study is about the impact of digital transformation on organization performance, specified to small and medium enterprises in the Apparel sector in Sri Lanka. Following are the inferences derived from the data analysis.

Demographic Background of the Sample

The research population is 7500 Small and Medium Enterprises in Western Province, Sri Lanka (which is specified to the apparel sector). The following table shows the demographic background of the sample.

Table 1: Summary of Sample Description

Demographic Characteristics		Percentage
Gender	Male	67.4%
	Female	32.6%
Age	18 – 25 years	1.9%
	26 – 35 years	22.7%
	36 – 45 years	62.5%
	Above 46	12.9%
Experience	Below 5 years	7.9%
	5 – 10 years	12.3%
	10 – 15 years	18.6%
	15 – 20 years	52.3%
	Over 20 years	8.8%

Source: Research data

Regression Analysis

In order to test hypotheses, regression analysis was conducted using the impact of four independent variables, compatibility, cost-effectiveness, trust and interactivity on the SME performance as the dependent variable. Before proceeding to the main analysis, normality, multicollinearity, heteroscedasticity and autocorrelation were

tested to confirm that the data fits the basic assumptions of the regression model, and all tests proved the fit of the basic model. The result of the regression analysis is mentioned below:

Table 2: Summary of the Regression Analysis

	ANOVA	Model Summary	Coefficient	
	Sig	R Square	B	Sig
Model	0.000	0.712		
Compatibility			0.050	0.006
Cost-effectiveness			0.119	0.039
Trust			0.093	0.002
Interactivity			0.853	0.000

Source: Research data

As per the above table, the overall model of the study is significant under the 5% significance level. The model's R square value depicts the dependent variable's predictability by all independent variables together. In this study, the R square value of the model is 0.712, where the IVs of this model can predict more than 71% of the variation in SME performance.

Moreover, IVs of the study, compatibility, cost-effectiveness, trust and interactivity significantly impact SME performance. According to the above table, a 1% change in compatibility affects a 5% change in SME performance, while a 1% change in cost-effectiveness affects an 11.9% change in SME performance. When considering the effect of trust on SME performance, it is identifiable that a 1% change will affect the 9.3% changes in SME performance. Further, the 1% change in interactivity will affect 85.3% changes in SME performance. The impact of all independent variables are significant under the 5% significant level and all hypothesis can be accepted. The following table depicts the summary of hypothesis testing.

Table 3: Summary of Hypothesis Testing

No	Hypothesis	Reason		Accepted/Rejected
		B	Sig	
H1	There is an impact of compatibility on the performance of small and medium enterprises.	0.050	0.006	Accepted



H2	There is an impact of cost-effectiveness on the performance of small and medium enterprises.	0.119	0.039	Accepted
H3	There is an impact of trust on the performance of small and medium enterprises.	0.093	0.002	Accepted
H4	There is an impact of interactivity on the performance of small and medium enterprises.	0.853	0.000	Accepted

Source: Research data

6. CONCLUSION

The current research is conducted to find out the impact of digital transformation on organization performance in small and medium enterprises in the apparel sector of Sri Lanka. This study continues with identified research problems in the apparel sector of small and medium enterprises in Sri Lanka. As discussed in early sections, the study continues with 365 apparel sector small and medium enterprises operating businesses in the Western province of Sri Lanka.

Their researcher found that the model is fitted with an R-squared value of 71.2%. With a significant value of less than 5%, it has been found that digital transformation impacts organisational performance. With coefficient value, it has identified that comparability, cost-effectiveness, trust, and interactivity is significantly impacted business performance. According to that, researchers accepted hypotheses H1, H2, H3 and H4. The current study consists of the past study of (Pereira et al., 2022), and the findings are in line with the studies which discussed the effect of technology on business performance, which concluded that technology adoption affects business performance positively (Gera and Gu, 2004; Paniagua and Sapena, 2014; Hakala and Kohtamäki, 2011). Further, a study in the Chinese context has found that digital transformation has both long-term and short-term positive impacts on financial performance (Wang et al., 2020). Alalawneh, Al-Omar, & Alkhatib, (2022) found that social media usage in business is positively associated with business performance in the restaurant industry, through the studies of (Wang et al., 2020) and (Alalawneh, Al-Omar, & Alkhatib, 2022) are completely similar to the findings of the present



study, which are consistent with the conclusion that digital transformation impacts SME performance.

Based on the inferences of the study, researchers can make some recommendations for SME owners. They can clearly outline the goals and objectives of your digital transformation. Determine what they want to achieve, whether it's improving customer experience, streamlining operations, expanding market reach, or something else. Ensure that top leadership is committed to the digital transformation process. It is required to ensure the support of top leadership, which is crucial in setting the tone, securing resources, and driving cultural change. By thoroughly assessing the current digital capabilities, processes, and systems, the current statutes can be assessed and identify areas that need improvement and prioritize them based on their impact on the business. Further, they can establish a strong online presence through social media, SEO, and targeted digital marketing campaigns. This can help you reach a wider audience and engage with customers more effectively.

The study has certain limitations. The study only used a quantitative cross-sectional method. Also, the study only focuses on small and medium enterprises in the Western province of Sri Lanka. Since the topic is important, there is a lack of research articles to observe. Based on the limitations of the present research, future research can expand to determine the impact of digital transformations on business performance. They can identify different variables, related to digital transformation. Continuing a qualitative study helps identify different authors' views. Further, future researchers can conduct longitudinal studies, which might give different results than the present study.

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