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Digital Branding Capability And Sustainability Marketing In Enhancing The Performance Of Creative Industry Smes In East Java

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Abstract

The rapid growth of the digital economy has encouraged Micro, Small, and Medium Enterprises (MSMEs) in the creative industry sector to strengthen their competitiveness through digital branding and sustainability-oriented marketing strategies. However, many creative MSMEs in East Java still face challenges in optimizing digital branding capability and implementing sustainability marketing to improve business performance in the digital era. Therefore, this study aims to analyze the effect of digital branding capability and sustainability marketing on SME performance through customer engagement as a mediating variable among creative industry MSMEs in East Java. This study employed a quantitative approach with an explanatory research design. Data were collected from 200 creative MSME owners in East Java using purposive sampling techniques. The analysis was conducted using Partial Least Squares Structural Equation Modeling (PLS-SEM) with the assistance of SmartPLS. The findings indicate that digital branding capability and sustainability marketing have positive and significant effects on customer engagement and SME performance. Furthermore, customer engagement significantly affects SME performance and partially mediates the relationship between digital branding capability, sustainability marketing, and SME performance. These findings suggest that strengthening digital branding capability and sustainability-oriented marketing strategies can improve customer relationships and enhance business competitiveness among creative MSMEs. Practically, this study provides managerial insights for creative MSMEs

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in developing effective digital branding strategies, strengthening sustainability communication, and improving customer engagement to support long-term business performance and competitive advantage in the digital economy.

Keywords: Digital Branding Capability, Sustainability Marketing, Customer Engagement, SME Performance, Creative Industry MSMEs

INTRODUCTION

The rapid advancement of digital technology has driven a substantial transformation in marketing activities and business models across various industrial sectors, including Micro, Small, and Medium Enterprises (MSMEs). Digital transformation has not only altered marketing communication patterns but has also reshaped how firms establish customer relationships, create brand value, and enhance business competitiveness in the digital economy era. Digital marketing is currently evolving beyond a mere promotional tool into a strategic capability that supports innovation and business sustainability among MSMEs (Dwivedi et al., 2021). Furthermore, Noer et al. (2025) explain that the integration of digital marketing and sustainable innovation has become a critical factor in enhancing business adaptability amid increasingly dynamic digital competition.

The creative industry has emerged as one of the strategic sectors contributing to national economic growth due to its characteristics that are strongly rooted in creativity, innovation, technology, and value-added products. In Indonesia, particularly in East Java, the development of creative industry MSMEs has increasingly been supported by the utilization of social media, marketplaces, and other digital platforms as instruments for product marketing and brand identity reinforcement. Nevertheless, many creative MSMEs continue to face challenges in establishing strong brand positioning within the digital environment. Most business actors remain focused on basic promotional activities and have not yet strategically and sustainably developed their digital branding capabilities.

In this context, digital branding capability has become an essential factor in improving MSME performance. Digital branding capability reflects a firm's ability to manage brand identity, create consistent digital communication, utilize social media effectively, and foster customer interaction through digital platforms. Apasrawirote and Muneesawang (2022) argue that digital marketing capability represents a firm's strategic ability to integrate digital resources in order to create competitive advantage and improve business performance. Other studies have also demonstrated that digital branding and

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digital marketing capabilities significantly influence customer engagement and MSME marketing performance (Jaya et al., 2026). Therefore, digital branding capability is no longer viewed merely as a promotional activity, but rather as an integral component of strategic business capability in responding to increasingly competitive digital market dynamics.

In addition to digital branding capability, sustainability marketing has also become an important concern in contemporary marketing strategies. Changes in consumer behavior, particularly the growing awareness of environmental issues, business ethics, and sustainability, have encouraged companies to integrate sustainability values into their marketing activities. Sustainability marketing is not solely oriented toward economic profit; it also emphasizes social responsibility, transparency, and sustainability in building long-term customer relationships. Fan et al. (2022) explain that digital transformation integrated with sustainability strategy is capable of enhancing sustainable business performance in the MSME sector. Moreover, sustainability marketing is considered capable of strengthening brand image and increasing customer trust toward firms.

On the other hand, customer engagement has become a strategic factor within the digital business environment because it reflects the level of customer involvement, interaction, and emotional connection with a brand. In the era of social commerce and social media, customer engagement has become one of the key indicators of the success of digital branding and sustainability marketing strategies. Customers with a high level of engagement tend to demonstrate stronger loyalty, actively interact with brands, and possess a greater likelihood of repurchasing products and recommending them to other consumers. Aityassine et al. (2021) explain that social media marketing has a significant influence on customer engagement and a firm's sustainable competitive advantage. Similarly, Rajiman et al. (2025) found that customer engagement plays an important role in improving MSME business performance through strengthening customer relationships and brand resonance capability.

Although numerous studies have examined digital marketing capability, sustainability, and customer engagement, several research gaps remain evident in the existing literature. First, most previous studies have focused on digital marketing in general and have not specifically examined digital branding capability as a strategic capability within the context of creative industry MSMEs. Second, studies on sustainability marketing have largely been investigated separately from digital branding capability. Third, research integrating digital branding capability and sustainability marketing in enhancing the performance of creative MSMEs in Indonesia, particularly in East Java,

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remains relatively limited. Furthermore, previous studies have rarely incorporated customer engagement as a mediating variable in explaining the relationship between digital branding capability, sustainability marketing, and MSME performance.

Based on the foregoing discussion, this study aims to analyze the influence of digital branding capability and sustainability marketing on the performance of creative industry MSMEs in East Java through customer engagement as a mediating variable. This study is expected to provide theoretical contributions to the development of digital marketing, sustainability marketing, and customer engagement literature within the creative MSME sector, while also offering practical contributions for business actors in designing sustainable digital branding strategies to improve business performance in the digital economy era.

LITERATURE REVIEW

Resource-Based View (RBV)

The Resource-Based View (RBV) is one of the principal theories used to explain how firms acquire and sustain competitive advantage through the effective management of strategic resources. Barney (1991) argues that firms are able to achieve competitive advantage when they possess resources that are valuable, rare, inimitable, and non-substitutable (VRIN). From the RBV perspective, organizational resources are not limited to physical assets but also encompass intangible resources such as technological capability, innovation, brand reputation, and digital marketing capability. In the era of the digital economy, a firm's ability to manage digital branding and sustainability marketing has become an essential component of its strategic capability. These capabilities enable firms to establish stronger customer relationships, enhance brand value, and expand their reach within digital markets. In the context of creative industry MSMEs, digital branding capability can be viewed as a strategic capability that supports product differentiation and brand positioning in the digital marketplace. Furthermore, sustainability marketing has emerged as a strategic orientation that supports business sustainability through the integration of economic, social, and environmental values into marketing activities. Sustainable marketing strategies are not solely directed toward improving profitability, but also toward building long-term customer trust and loyalty. Therefore, the Resource-Based View provides a relevant theoretical foundation for explaining the relationships among digital branding capability, sustainability marketing, customer engagement, and MSME performance.

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Digital Branding Capability

Concept of Digital Branding Capability

Digital Branding Capability refers to a firm's ability to develop, manage, and strengthen brand identity through the utilization of digital technologies and online platforms. This concept has evolved alongside the increasing use of digital media as a medium for marketing communication and customer interaction. According to Apasrawirote and Muneesawang (2022), digital marketing capability represents a firm's ability to leverage digital technologies to enhance the effectiveness of marketing strategies, establish customer relationships, and improve business performance. In the context of branding, such capability includes the management of brand visual identity, digital content quality, interactive communication, social media management, and the ability to adapt to the rapid evolution of digital platforms. Digital Branding Capability has become increasingly important for creative industry MSMEs because competition in digital markets is determined not only by product quality, but also by the strength of brand image and customer experience within the digital environment. Digital branding capability enables firms to create stronger brand differentiation through creative content, digital storytelling, and interactive customer experiences. Dwivedi et al. (2021) explain that the advancement of digital and social media marketing has transformed the pattern of communication between firms and customers into a more interactive and customer-oriented approach. Therefore, digital branding capability is viewed as a strategic capability that can enhance customer engagement and strengthen business competitiveness.

Digital Branding Capability and Customer Engagement

Customer Engagement refers to the level of customers' emotional, cognitive, and behavioral involvement with a brand. Within the digital business environment, customer engagement has become one of the key indicators of the success of digital branding strategies because it reflects the quality of the relationship between customers and firms. Digital Branding Capability enables firms to establish more interactive and personalized digital communication with customers. Creative digital content, consistency of brand identity, and a firm's ability to utilize social media effectively can enhance customer participation in the company's digital activities. From the perspective of the Resource-Based View, digital branding capability is considered an intangible strategic resource capable of creating long-term customer relationships through positive digital experiences. The stronger a firm's capability in managing digital branding, the higher the level of

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customer engagement toward the brand. Jaya et al. (2026) found that digital marketing capability has a positive influence on customer engagement among digital-based MSMEs. Similarly, Rajiman et al. (2025) demonstrated that brand resonance capability is able to enhance customer engagement through social media and digital platforms. Furthermore, Djohan et al. (2025) explain that digital branding and customer engagement have a significant relationship in improving the performance of digital-based MSMEs. These findings indicate that strong digital branding is capable of creating customers' emotional attachment to a brand. Based on the theoretical arguments and findings of previous studies, it can be concluded that MSMEs' capability in developing digital branding will improve the quality of customer interaction and strengthen customer engagement. Therefore, the following hypothesis is proposed:

H1: Digital Branding Capability has a positive effect on Customer Engagement.

Digital Branding Capability and MSME Performance

Digital Branding Capability not only plays a role in enhancing customer interaction, but also contributes significantly to improving business performance. A firm's ability to establish a strong brand identity within the digital environment enables it to increase brand awareness, expand market reach, and strengthen customer loyalty. In the context of creative industry MSMEs, digital branding has become a crucial factor because creative products are highly dependent on symbolic value, aesthetics, and emotional value embedded within the brand. Strong digital branding capability assists MSMEs in creating stronger product positioning compared to competitors. Apasrawirote and Muneesawang (2022) explain that digital capability can improve business performance through the effectiveness of digital marketing and the strengthening of customer relationships. Similarly, Jaya et al. (2026) found that digital marketing capability has a significant influence on MSME marketing performance. Furthermore, Noer et al. (2025) explain that digital marketing capability and digital innovation have become essential factors in enhancing the competitiveness and sustainability of MSMEs in the digital economy era. Based on the perspective of the Resource-Based View, digital branding capability represents a strategic capability capable of generating competitive advantage and improving business performance. The stronger the digital branding capability of MSMEs, the greater their ability to enhance sales performance, customer loyalty, and market expansion. Therefore, the following hypothesis is proposed:

H2: Digital Branding Capability has a positive effect on MSME Performance.

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Sustainability Marketing

Concept of Sustainability Marketing

Sustainability Marketing refers to a marketing strategy that integrates economic, social, environmental, and business ethical aspects into corporate marketing activities. This concept has evolved in response to increasing consumer awareness regarding sustainability issues and corporate social responsibility. According to Philip Kotler (2011), sustainability marketing is not solely intended to achieve economic profit, but also to create a balance among profit, people, and planet. Sustainable marketing strategies emphasize the importance of ethical values, transparency, and social responsibility in building long-term relationships with customers. In the context of creative industry MSMEs, sustainability marketing can be implemented through the use of environmentally friendly materials, ethical branding, product transparency, green communication, and social activities that support business sustainability. Fan et al. (2022) explain that the integration of digital transformation and sustainability strategy is capable of improving firms' sustainable business performance. In addition, sustainability marketing also helps firms build a positive corporate image and enhance customer trust. Noer et al. (2025) further explain that sustainable innovation and digital marketing are important factors in improving MSME competitiveness in the digital economy era. Therefore, Sustainability Marketing is viewed as a strategic orientation that supports business sustainability and performance.

Sustainability Marketing and Customer Engagement

Changes in modern consumer behavior indicate that customers are increasingly concerned with ethical values, environmental awareness, and corporate social responsibility in the purchasing decision-making process. Consequently, firms implementing sustainability marketing are more likely to establish emotional relationships with customers. From the perspective of relationship marketing, Sustainability Marketing enables firms to create emotional connections through the communication of sustainability values and corporate social responsibility. Customers who possess positive perceptions toward a firm's sustainability practices tend to interact more actively with and support the brand. Aityassine et al. (2021) explain that social media marketing integrated with social values can increase customer engagement and a firm's sustainable competitive advantage. In addition, Fan et al. (2022) found that sustainability strategy is capable of strengthening customer relationships and increasing customer loyalty. In creative industry MSMEs, sustainability marketing can enhance customer engagement

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through digital communication that emphasizes sustainability values, environmentally friendly products, and corporate social activities. Such strategies are capable of increasing customer involvement in firms' digital activities. Based on the foregoing discussion, it can be argued that Sustainability Marketing plays an important role in enhancing customers' engagement toward brands. Therefore, the following hypothesis is proposed:

H3: Sustainability Marketing has a positive effect on Customer Engagement.

Sustainability Marketing and MSME Performance

Sustainability Marketing not only affects customer relationships, but also contributes to improving firms' business performance. Sustainable marketing strategies are capable of enhancing corporate image, building customer trust, and strengthening long-term customer loyalty. In the context of creative MSMEs, sustainability marketing can serve as a strategic differentiation factor that distinguishes a firm's products from those of competitors. Modern consumers tend to prefer products that embody sustainability values and social responsibility. Fan et al. (2022) found that sustainability strategy has a positive influence on firms' sustainable business performance. Furthermore, Noer et al. (2025) demonstrated that sustainable innovation and digital marketing are capable of improving MSME business competitiveness. Based on the perspective of the Resource-Based View, sustainability marketing represents a strategic orientation capable of generating value creation and competitive advantage for firms. The better the implementation of sustainability marketing, the greater the ability of MSMEs to improve business performance. Therefore, the following hypothesis is proposed:

H4: Sustainability Marketing has a positive effect on MSME Performance.

Customer Engagement

Concept of Customer Engagement

Customer Engagement refers to the level of customers' emotional, cognitive, and behavioral involvement with a brand or company. The concept of customer engagement has developed alongside the increasing digital interaction between firms and customers through social media and online platforms. Linda D. Hollebeek and Roderick J. Brodie et al. (2011) explain that customer engagement is a psychological process reflecting customers' interactive experiences with brands through digital activities and emotional relationships with firms. Within the digital business environment, customer engagement can be manifested through customer activities such as commenting, sharing content,

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posting reviews, following companies' social media activities, and engaging in repeat purchases. Customer Engagement has become an important factor for creative industry MSMEs because customer involvement is capable of increasing loyalty, strengthening customer relationships, and generating positive word of mouth.

Customer Engagement and MSME Performance

In the digital era, Customer Engagement is regarded as one of the critical factors determining business success. Customers with high engagement levels tend to exhibit stronger loyalty, actively promote brands, and possess a greater likelihood of making repeat purchases. Relationship Marketing Theory explains that long-term relationships between firms and customers enhance business value through customer loyalty and improved customer retention. Rajiman et al. (2025) demonstrated that customer engagement has a positive influence on MSME business performance. Likewise, Aityassine et al. (2021) explain that customer engagement is capable of enhancing firms' sustainable competitive advantage. In creative industry MSMEs, customer engagement can improve business performance through increased customer loyalty, broader digital networking, and word-of-mouth promotion on social media platforms. Based on the theoretical arguments and previous empirical findings, it can be concluded that the higher the level of customer engagement, the better the performance of MSMEs. Therefore, the following hypothesis is proposed:

H5: Customer Engagement has a positive effect on MSME Performance.

The Mediating Role of Customer Engagement

Customer Engagement is viewed as an important mechanism explaining how Digital Branding Capability and Sustainability Marketing improve MSME performance. In the digital business context, the success of branding and sustainability strategies is not determined solely by firms' ability to build brand image, but also by their capability to generate customer engagement. Digital Branding Capability enables firms to create more interactive digital communication, thereby increasing customer engagement toward brands. Meanwhile, Sustainability Marketing is capable of building customers' emotional attachment through sustainability values and corporate social responsibility. Customers with high engagement levels tend to be more loyal, actively interact with brands, and possess a greater likelihood of repurchasing and recommending products to other customers. Therefore, Customer Engagement serves as an important mediating variable in explaining the influence of digital branding capability and sustainability marketing on

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MSME performance. Rajiman et al. (2025) demonstrated that customer engagement is capable of mediating the relationship between digital marketing orientation and MSME business performance. Other studies also explain that customer engagement represents a strategic factor in enhancing the effectiveness of digital marketing on business performance. Based on these arguments, the following hypotheses are proposed:

H6: Customer Engagement mediates the effect of Digital Branding Capability on MSME Performance.

H7: Customer Engagement mediates the effect of Sustainability Marketing on MSME Performance.

Conseptual Framework

This study is developed based on the perspective of the Resource-Based View, which explains that firms can achieve competitive advantage through the effective management of strategic resources and capabilities. In the context of creative industry MSMEs, Digital Branding Capability and Sustainability Marketing are viewed as strategic capabilities that are capable of enhancing Customer Engagement and business performance. Digital Branding Capability reflects the ability of MSMEs to establish digital brand identity, manage digital marketing communication, create creative content, and utilize social media effectively in building customer relationships. Strong digital branding capability enables MSMEs to enhance customer interaction, expand market reach, and strengthen brand positioning within the digital environment. Meanwhile, Sustainability Marketing refers to a marketing strategy that integrates sustainability values, social responsibility, business ethics, and environmental awareness into firms' marketing activities. The implementation of sustainability marketing enables MSMEs to build a positive corporate image, increase customer trust, and create emotional relationships with consumers. Within the digital business environment, the success of digital branding and sustainability marketing strategies is not determined solely by firms' ability to establish brand image, but also by their capability to generate Customer Engagement. Customer engagement reflects the level of customers' emotional, cognitive, and behavioral involvement with a brand through digital activities. Customers with high levels of engagement tend to demonstrate stronger loyalty, actively interact with brands, and possess a greater likelihood of engaging in repeat purchases and recommending products to other consumers. Therefore, customer engagement is considered to play a significant role in improving the performance of creative industry MSMEs. MSME performance in this study reflects the level of business success in achieving

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organizational objectives, such as increased sales, customer growth, market expansion, profitability, and customer loyalty. Based on theoretical arguments and findings from previous studies, this study develops a conceptual model explaining that Digital Branding Capability and Sustainability Marketing have direct effects on both Customer Engagement and MSME performance. Furthermore, customer engagement is positioned as a mediating variable that explains the mechanism underlying the relationship between digital branding capability, sustainability marketing, and the performance of creative industry MSMEs in East Java.

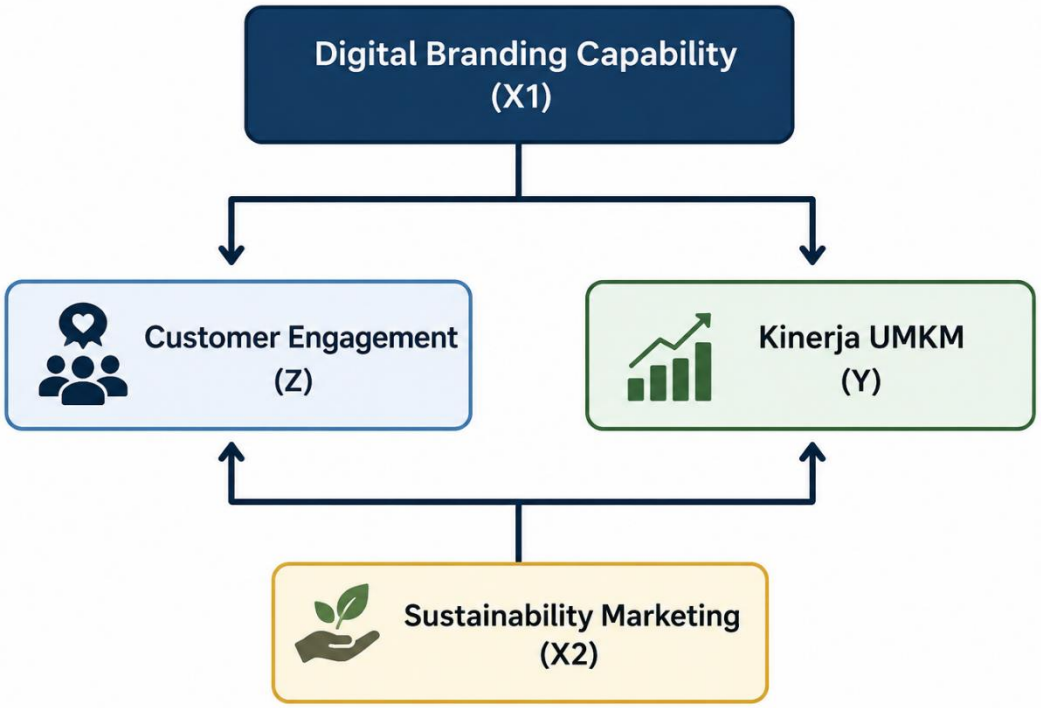


Figure 1. Conseptual Framework

RESEARCH METHOD

Population and Sample

This study employed a quantitative approach with an explanatory research design to analyze the influence of Digital Branding Capability and Sustainability Marketing on SME performance through Customer Engagement as a mediating variable among creative industry MSMEs in East Java. The population of this study consisted of all

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creative industry MSME actors in East Java that had utilized digital media as a tool for business marketing and branding activities, particularly within the sectors of creative fashion, creative culinary businesses, handicrafts, handmade products, batik, and digital-based creative businesses.

The sampling technique applied in this study was purposive sampling because respondents were required to meet specific characteristics relevant to the research objectives. The criteria included: (1) creative industry MSME actors located in East Java, (2) possessing business social media accounts or digital platforms, (3) actively conducting digital marketing activities, and (4) operating the business for a minimum of one year.

The determination of sample size referred to the recommendation of Hair et al. (2022), which states that the minimum sample size in SEM-PLS analysis should range from five to ten times the number of research indicators. Considering the total number of indicators used in this study, a total of 200 respondents representing creative industry MSMEs in East Java were selected in order to improve the accuracy and stability of the research model. Research data were collected through the distribution of online questionnaires using Google Forms during the data collection period.

Sample Characteristics

The characteristics of respondents in this study were used to provide a general overview of the profile of creative industry MSMEs as the research objects, as well as the respondents' level of digital adaptation in branding and digital marketing activities.

Table 1. Sample Characteristics

Characteristics	Category
Business Sector	Fashion Creative, Culinary Creative, Craft/Handmade, Batik, Digital Creative Business
Business Duration	1–3 Years, 4–6 Years, >6 Years
Number of Employees	1–5 Employees, 6–10 Employees, >10 Employees
Digital Platforms Used	Instagram, TikTok, Facebook, Marketplace, Website
Business Scale	Micro, Small, Medium

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Measurement

This study utilized primary data collected through the distribution of questionnaires to 200 creative industry MSME actors in East Java. All measurement items were adapted from previous studies that had demonstrated established validity and reliability and were measured using a five-point Likert scale ranging from 1 = strongly disagree to 5 = strongly agree.

The variable of Digital Branding Capability was adapted from the concept of digital marketing capability developed by Apasrawirote and Muneesawang (2022), which includes digital brand identity consistency, digital content quality, social media management, digital customer interaction, and digital platform adaptability.

The variable of Sustainability Marketing was adapted from the concepts of sustainable marketing and sustainable business strategy developed by Fan et al. (2022) and Philip Kotler (2011), encompassing sustainability communication, ethical marketing, product transparency, environmental concern, and corporate social responsibility. The variable of Customer Engagement was adapted from Roderick J. Brodie et al. (2011), including customer involvement, customer participation, digital interaction, emotional attachment, and digital customer loyalty. Meanwhile, the SME performance variable was adapted from Augusty Ferdinand (2014) and related studies on SME performance, which include sales growth, customer growth, profitability, market expansion, and customer loyalty. Prior to the large-scale distribution of questionnaires, the research instrument was first tested through a pilot study to ensure the clarity of questionnaire items and minimize potential measurement bias.

Common Method Bias (CMB)

Since this study employed a self-reported questionnaire with a single respondent source, testing for common method bias (CMB) was conducted to minimize potential measurement bias. Several procedural remedies were implemented to reduce the likelihood of CMB, including maintaining respondent anonymity, ensuring that there were no right or wrong answers, constructing simple and easily understandable questionnaire items, and separating item arrangements among variables to reduce respondents' consistency motives.

In addition to these preventive procedures, statistical testing for common method bias was conducted using Harman's Single Factor Test. According to Podsakoff et al. (2003), if a single factor does not explain more than 50% of the total variance, common method bias is not considered a serious issue within the study. Furthermore, this study

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also evaluated the full collinearity variance inflation factor (VIF) within the PLS model. VIF values below 3.3 indicate that the research model is free from potential common method bias (Kock, 2015).

Analysis Procedure

This study employed Partial Least Squares Structural Equation Modeling (PLS-SEM) using SmartPLS to analyze the relationships among the research variables. PLS-SEM was selected because it is capable of simultaneously analyzing complex relationships among latent variables, is suitable for prediction-oriented and theory development research models, does not require strict assumptions of data normality, and effectively tests mediating relationships.

The data analysis was conducted through several stages. First, descriptive analysis was performed to describe respondent characteristics and the distribution of research responses. Second, measurement model evaluation (outer model) was conducted to assess convergent validity, discriminant validity, composite reliability, and Cronbach's alpha. Third, structural model evaluation (inner model) was carried out to evaluate the coefficient of determination (R^2), predictive relevance (Q^2), effect size (f^2), and overall model goodness of fit. Finally, hypothesis testing was performed using the bootstrapping procedure by examining t-statistics and p-values. In addition, the mediating effect of Customer Engagement was tested through indirect effect analysis in PLS-SEM to evaluate the indirect relationships among the research variables.

RESULT AND DISCUSSION

RESULT

Respondent Profile

This study involved 200 creative industry MSME actors in East Java who actively utilized digital media in their marketing and business branding activities. The respondent characteristics indicate that the majority of MSMEs operated within the sectors of creative fashion, creative culinary businesses, and craft/handmade products, with dominant utilization of digital platforms such as Instagram, TikTok, and online marketplaces to support digital marketing activities. Most respondents had also operated their businesses for more than three years, indicating that the MSMEs possessed considerable experience in managing digital businesses and establishing customer relationships through online media.

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These characteristics suggest that creative industry MSMEs in East Java have begun adapting to digital transformation, particularly in implementing Digital Branding Capability and Sustainability Marketing as strategic approaches to improving business competitiveness.

Table 2. Respondent Characteristics

Characteristics	Category	Percentage
Business Sector	Fashion Creative	32%
	Culinary Creative	38%
	Craft/Handmade	20%
	Batik and Others	10%
Business Duration	1–3 Years	29%
	4–6 Years	41%
	>6 Years	30%
Digital Platforms Used	Instagram	40%
	TikTok	28%
	Marketplace	20%
	Facebook and Website	12%
Business Scale	Micro	54%
	Small	33%
	Medium	13%

Measurement Model Evaluation (Outer Model)

The outer model evaluation was conducted to assess the validity and reliability of the research constructs through convergent validity, discriminant validity, composite reliability, and Cronbach's alpha.

Convergent Validity

Convergent validity was examined by evaluating the outer loading values and the Average Variance Extracted (AVE). According to Hair et al. (2022), indicators are considered valid when they possess loading factor values above 0.70 and AVE values greater than 0.50.

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The results of the analysis indicate that all indicators associated with the variables of Digital Branding Capability, Sustainability Marketing, Customer Engagement, and SME performance demonstrated loading factor values above 0.70, thereby satisfying the criteria for convergent validity. Furthermore, all constructs exhibited AVE values exceeding 0.50, indicating that the research variables were capable of adequately explaining the variance of their respective indicators.

Table 3. Convergent Validity and Reliability

Variable	Outer Loading	AVE	Composite Reliability	Cronbach's Alpha
Digital Branding Capability	0.742–0.891	0.681	0.914	0.883
Sustainability Marketing	0.731–0.876	0.664	0.908	0.872
Customer Engagement	0.755–0.903	0.702	0.922	0.894
SME Performance	0.748–0.889	0.689	0.917	0.887

Based on these results, all research constructs were declared valid and reliable.

Discriminant Validity

Discriminant validity was assessed using the Fornell-Larcker Criterion and the Heterotrait-Monotrait Ratio (HTMT). The results indicate that all constructs possessed square root AVE values greater than the correlations with other constructs, while all HTMT values were below the recommended threshold of 0.90. Therefore, all research variables satisfied the criteria for discriminant validity.

Table 4. Discriminant Validity – Fornell-Larcker Criterion

Construct	DBC	SM	CE	SP
Digital Branding Capability (DBC)	0.825			
Sustainability Marketing (SM)	0.612	0.815		
Customer Engagement (CE)	0.684	0.645	0.838	
SME Performance (SP)	0.691	0.658	0.734	0.830

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Table 5. HTMT Ratio

Construct	DBC	SM	CE	SP
DBC	-			
SM	0.742	-		
CE	0.801	0.776	-	
SP	0.824	0.791	0.861	-

Therefore, the results of the measurement model evaluation demonstrate that all research constructs satisfy the required criteria of validity and reliability.

Structural Model Evaluation (Inner Model)

The inner model evaluation was conducted to assess the capability of the research model in explaining the relationships among latent variables through the coefficient of determination (R^2), predictive relevance (Q^2), and effect size (f^2). The results indicate that Customer Engagement obtained an R^2 value of 0.587, suggesting that Digital Branding Capability and Sustainability Marketing were able to explain 58.7% of the variance in customer engagement. In addition, the R^2 value for SME performance was 0.648, indicating that the research model possessed strong predictive capability in explaining the business performance of creative industry MSMEs in East Java.

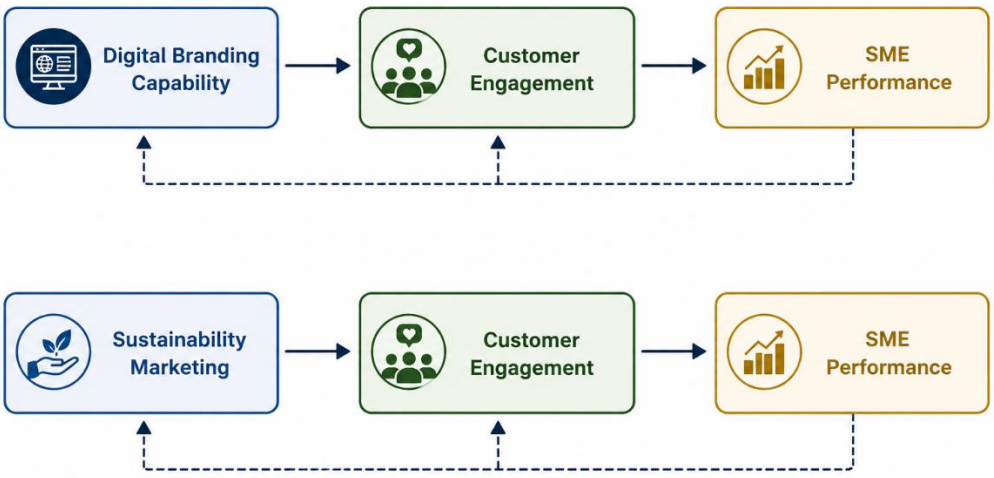
The predictive relevance (Q^2) values, which were greater than zero, indicate that the research model demonstrated satisfactory predictive relevance. Furthermore, the effect size (f^2) results reveal that Digital Branding Capability and Sustainability Marketing contributed significantly to both Customer Engagement and SME performance.

Table 6. Structural Model Evaluation

Variable	R^2	Q^2	Interpretation
Customer Engagement	0.587	0.401	Moderate
SME Performance	0.648	0.472	Moderate–Strong

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Description → Direct influence
- - - Feedback or indirect influence

Figure 2. Structural Model

Hypothesis Testing

Hypothesis testing was conducted using the bootstrapping procedure in SmartPLS by examining the path coefficients, t-statistics, and p-values.

Table 7. Hypothesis Testing Results

Hypothesis	Relationship	Beta	t-value	p-value	Result
H1	Digital Branding Capability → Customer Engagement	0.391	5.872	0.001	Supported
H2	Digital Branding Capability → SME Performance	0.284	4.215	0.001	Supported
H3	Sustainability Marketing → Customer Engagement	0.352	5.144	0.001	Supported
H4	Sustainability Marketing → SME Performance	0.267	3.987	0.001	Supported
H5	Customer Engagement → SME Performance	0.421	6.337	0.001	Supported

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H6	DBC → CE → SME Performance	0.165	4.011	0.001	Supported
H7	SM → CE → SME Performance	0.148	3.765	0.001	Supported

The results of the hypothesis testing indicate that all hypotheses proposed in this study were supported, as all relationships demonstrated t-statistics values above 1.96 and p-values below 0.05.

Table 8. Summary Data for the Mediation Model

Path	Direct Effect	Indirect Effect	Mediation Type
DBC → SME Performance	Significant	Significant	Partial Mediation
SM → SME Performance	Significant	Significant	Partial Mediation

DISCUSSION

The findings of this study provide new contributions toward addressing several important research gaps that remain insufficiently explored in the existing literature. One of the primary contributions lies in the inconsistency of the mediating role of Dynamic Capabilities (DC) within the SME context compared to large corporations. While previous studies, such as those conducted by Indriastuti and Kartika (2022) and Al Jabri et al. (2024), demonstrated that DC functions as a full mediator in the relationship between digitalization and organizational performance, the present study reveals that, among SMEs in East Java, DC operates merely as a complementary variable. This discrepancy may be explained by the limited resources of SMEs, which tend to rely heavily on community-based local networks to support innovation, as well as by the complexity of local institutional environments, where government initiatives such as the Smart Province 5.0 program encourage reactive innovation rather than innovation driven through systematically developed dynamic capabilities. These findings suggest that institutional logic exerts a stronger influence than market logic in shaping SMEs' innovative behavior.

From a theoretical perspective, these findings challenge the universality of Dynamic Capabilities Theory in the context of developing SMEs and reinforce the argument proposed by Mele et al. (2024) that dynamic capabilities are inherently contextual and require integration with institutional theories to enhance their explanatory relevance. Furthermore, this study reveals the fragmented role of Digital Financial Literacy (DFL) within the innovation model. Although previous studies, including Mishra

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and Kiran (2025) and Abdurrahman et al. (2024), positioned DFL as a key antecedent in the development of DC, the results of this study indicate that DFL only significantly influences the formation of DC (β = 0.266) and does not directly affect innovative performance. This discrepancy may be attributed to the incomplete internalization of digital financial management principles among SME actors. Data from the East Java Financial Services Authority (OJK East Java, 2023) indicate that although 89% of SMEs have adopted digital payment systems, only approximately 23% adequately understand digital cash flow management. This condition is further aggravated by the underdeveloped supporting ecosystem, including limited access to digital-based financing schemes, such as Digital People's Business Credit (Digital KUR), and inadequate technological infrastructure. Therefore, future studies should consider incorporating digital ecosystem moderators, such as fintech availability and infrastructural support, into the analytical framework.

This study also identifies the dualistic role of Strategic Agility (SA), which, on the one hand, demonstrates a direct influence on innovative performance (β = 0.229), yet, on the other hand, fails to exert a significant indirect effect through DC, contrary to the assumptions proposed in previous studies such as Bhatti et al. (2022). This finding is consistent with the results reported by Sarwar et al. (2024) and can be explained by the distinctive characteristics of SMEs in East Java. Most SMEs operating in creative sectors, such as batik and culinary industries, rely more heavily on agility rooted in local networking systems including collaboration with regional state-owned enterprises than on data-driven digital platforms. Consequently, the form of SA identified in this context is more accurately characterized as improvisational agility, referring to rapid responses to market changes, rather than analytical agility, which depends primarily on systematic data analysis, as commonly observed in large corporations.

Furthermore, Transformational Change Readiness (TCR) emerged as the most dominant variable, influencing both the development of DC (β = 0.331) and innovative performance directly (β = 0.250). These findings support the study conducted by Octasylva et al. (2022) while also providing a new perspective by demonstrating that readiness for change within SMEs is not necessarily grounded in formal management systems but is often stimulated by charismatic local leaders, commonly referred to as local heroes. In addition, external interventions, particularly government-led capacity-building programs such as "SMEs Go Digital," play a crucial role in fostering transformational readiness rather than relying solely on internal initiatives from SME actors themselves.

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This study also offers a critical perspective on the limitations of the Resource-Based View (RBV) in explaining SMEs' competitive advantage. Contrary to the fundamental assumptions of RBV, which emphasize the importance of internal resources, the findings of this study demonstrate that the competitive advantage of SMEs in East Java is largely shaped through institutional collaboration, such as partnerships with regional state-owned enterprises including the Jawa Timur Industrial and Trading Company, which provide access to external resources without requiring SMEs to independently develop such capabilities. Moreover, innovative initiatives among SMEs often emerge not from strategic business calculations but rather from social pressures and community norms, such as the responsibility to preserve local cultural heritage. This finding reinforces the importance of incorporating civic logic as a critical dimension in the development of knowledge-based dynamic capabilities theory, as suggested by Mele et al. (2024).

CONCLUSION

The Effect of Digital Branding Capability on Customer Engagement

The results of this study indicate that Digital Branding Capability has a positive effect on Customer Engagement. These findings demonstrate that MSMEs' capability in managing digital brand identity, creating creative content, and establishing interactive communication through social media is capable of increasing customer engagement with brands. From the perspective of the Resource-Based View, digital branding capability represents a strategic capability that can create competitive advantage through strengthening customer relationships and enhancing customers' digital experiences. The findings of this study support the work of Apasrawirote and Muneesawang (2022), who explain that digital marketing capability plays an important role in increasing customer interaction and business performance.

These findings also reinforce the studies of Noer et al. (2025) and Rajiman et al. (2025), which state that digital branding capability is able to enhance brand resonance and customer engagement among digital-based MSMEs.

The Effect of Sustainability Marketing on Customer Engagement

The results indicate that Sustainability Marketing has a positive effect on Customer Engagement. These findings suggest that the implementation of sustainable marketing strategies is capable of increasing customers' emotional attachment toward brands. Modern consumers tend to be more attracted to companies that demonstrate concern for

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environmental sustainability, business ethics, and social responsibility. Therefore, sustainability marketing has become an important factor in building long-term relationships with customers.

The findings of this study support Fan et al. (2022), who state that sustainability strategy is capable of strengthening customer relationships and improving firms' sustainable business performance.

The Effect of Digital Branding Capability on SME Performance

This study demonstrates that Digital Branding Capability has a positive effect on the performance of creative industry MSMEs in East Java. Digital branding capability enables MSMEs to increase brand awareness, expand digital markets, and strengthen customer loyalty, thereby contributing to improved business performance. These findings support the perspective of the Resource-Based View, which explains that firms' digital capabilities constitute intangible resources capable of creating competitive advantage in the digital economy era.

The Effect of Sustainability Marketing on SME Performance

The results indicate that Sustainability Marketing has a positive effect on SME performance. The implementation of sustainability marketing assists firms in improving brand image, building customer trust, and strengthening customer loyalty. These findings demonstrate that sustainability marketing functions not only as a business ethics strategy, but also as a strategic orientation that supports the sustainability and competitiveness of creative MSMEs.

The Effect of Customer Engagement on SME Performance

The findings reveal that Customer Engagement has a positive effect on SME performance. Customers with high levels of engagement toward brands tend to exhibit stronger loyalty, actively engage in repeat purchases, and provide positive word-of-mouth promotion to other customers. These findings reinforce Relationship Marketing Theory, which explains that long-term relationships with customers are capable of improving firms' business performance.

The Mediating Role of Customer Engagement

This study also found that Customer Engagement is capable of mediating the effects of Digital Branding Capability and Sustainability Marketing on SME performance.

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These findings indicate that the success of digital branding and sustainability marketing strategies depends not only on firms' capability to establish brand image, but also on their ability to create customer engagement. Customer engagement therefore becomes an important mechanism linking digital marketing strategies with improved business performance among creative industry MSMEs in East Java.

CONCLUSION

This study aimed to analyze the influence of Digital Branding Capability and Sustainability Marketing on SME performance through Customer Engagement among creative industry MSMEs in East Java. The findings demonstrate that digital branding capability and sustainability marketing have positive and significant effects on both customer engagement and SME performance. In addition, customer engagement was also found to have a positive effect on improving the performance of creative industry MSMEs. The findings indicate that MSMEs' capability in managing digital branding through social media utilization, creative content development, and digital customer interaction is capable of increasing customer engagement and strengthening firms' business performance. On the other hand, the implementation of sustainability marketing through sustainability communication, product transparency, and social responsibility is also capable of enhancing customers' emotional attachment toward brands while simultaneously strengthening MSMEs' business competitiveness in the digital economy era. This study further reveals that Customer Engagement acts as a mediating variable explaining the relationship between Digital Branding Capability, Sustainability Marketing, and SME performance. These findings indicate that the success of digital marketing strategies is determined not only by firms' capability in building digital brand image, but also by their ability to establish interactive and sustainable customer engagement. From a theoretical perspective, this study contributes to the development of the literature on digital marketing, sustainability marketing, and customer engagement by integrating the perspective of the Resource-Based View within the context of creative industry MSMEs in Indonesia. The findings reinforce the view that digital capability and sustainability orientation constitute strategic resources capable of creating competitive advantage for MSMEs in responding to digital economic transformation. From a practical perspective, the findings provide important implications for creative industry MSME actors to strengthen digital branding strategies through the optimization of social media, the development of creative content, and the enhancement of digital customer interaction. In addition, the implementation of sustainability marketing should be reinforced through

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sustainability communication, product transparency, and social responsibility in order to improve customer loyalty and sustainable business performance. This study has several limitations, including the use of a cross-sectional approach and the research focus limited to creative industry MSMEs in East Java, which restricts the generalizability of the findings. Therefore, future studies are recommended to extend the research model by incorporating moderating variables such as digital orientation, innovation capability, or environmental uncertainty in order to further develop the literature on digital marketing and sustainability marketing within the MSME context in the digital era.

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