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# Digitalization, Product Innovation, And SME Sustainability: The Mediating Role Of Competitive Advantage In Local Wisdom-Based Enterprises

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**Abstract**

*The sustainability of small and medium-sized enterprises (SMEs) has become an increasingly important issue amid rapid technological change and intensifying market competition. This study examines the effects of digitalization and product innovation on the sustainability of local wisdom-based SMEs, with competitive advantage serving as a mediating variable. Drawing on the Resource-Based View (RBV) and Dynamic Capabilities Theory, the study investigates how digital and innovation capabilities contribute to sustainable business performance.A quantitative approach was employed using survey data collected from 200 owners and managers of local wisdom-based SMEs in Banjarmasin, Indonesia. The data were analyzed using Partial Least Squares Structural Equation Modeling (PLS-SEM). The results reveal that digitalization significantly influences competitive advantage (β = 0.412, p < 0.001) and SME sustainability (β = 0.265, p < 0.001). Product innovation also exerts significant positive effects on competitive advantage (β = 0.438, p < 0.001) and sustainability (β = 0.187, p = 0.001). Furthermore, competitive advantage has the strongest direct effect on sustainability (β = 0.523, p < 0.001) and partially mediates the relationships between digitalization, product innovation, and sustainability. The findings suggest that the sustainability of local wisdom-based SMEs depends not only on the possession of unique cultural resources but also on the ability to transform these resources into market value through digitalization and continuous innovation. This study contributes to the literature by integrating RBV and Dynamic Capabilities Theory to explain how competitive advantage functions as a strategic mechanism linking organizational capabilities to*



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*sustainability. The findings also provide practical guidance for SME owners and policymakers seeking to foster sustainable local economic development.*

**Keywords: digitalization; product innovation; competitive advantage; SME sustainability; local wisdom**

## INTRODUCTION

In many developing economies, the sustainability of small and medium-sized enterprises (SMEs) is increasingly threatened by rapid technological disruption, changing consumer behavior, and intensified market competition. These challenges are particularly significant for local wisdom-based SMEs, whose competitive position depends not only on economic performance but also on their ability to preserve cultural identity while adapting to contemporary market demands. In Indonesia, SMEs account for more than 99% of all business entities and contribute substantially to employment generation and national economic growth ( Kementerian Koperasi dan UKM, 2024). Beyond their economic contribution, many SMEs play a crucial role in preserving local culture, traditional knowledge, and indigenous craftsmanship. These enterprises represent an important vehicle for maintaining cultural heritage while simultaneously supporting community-based economic development.

However, the increasing dominance of digital technologies and rapidly evolving market dynamics have created new challenges for the sustainability of local wisdom-based SMEs. While these businesses possess unique cultural resources that differentiate them from competitors, many still face difficulties in adopting digital technologies, expanding market access, and maintaining long-term competitiveness. Consequently, ensuring the sustainability of local wisdom-based SMEs has become a strategic concern for both policymakers and business practitioners seeking to promote inclusive and sustainable economic development.

An SME's sustainability goes well beyond its financial returns; the term points to a firm's ability to keep itself viable for the long haul, adapt as its surroundings change, and produce value for stakeholders over the years (Rosati & Faria, 2019). This understanding maps closely onto the Triple Bottom Line framework, which underscores the blending of economic, social, and environmental aims within the choices an organization makes (Elkington, 1997). When an SME is grounded in local wisdom, sustainability further entails guarding cultural heritage, handed-down knowledge, and local identity while the enterprise continues to compete.



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Throughout Indonesia, digital transformation among SMEs has gathered considerable momentum in the last few years, yet how digitally ready firms are differs sharply from one sector or region to another (BPS Kalimantan Selatan, 2024). Within Banjarmasin, locally rooted SMEs continue to wrestle with taking on digital tools, reaching new markets, and surviving over time, despite the distinctive cultural endowments and singular products they possess. Such hurdles weigh most heavily on businesses turning out Sasirangan textiles, traditional Banjar food, handicrafts, and herbal goods, where proprietors must square the preservation of culture with the demands of a changing market.

In the present-day commercial setting, digitalization has risen to become a leading engine of competitiveness and sustainability. The concept refers to folding digital technologies into operational processes, interactions with customers, and the work of creating value (Verhoef et al., 2021). Taking on e-commerce platforms, promotion via social media, digital payment instruments, and cloud-based systems has transformed the manner in which SMEs operate and compete. Studies done earlier suggest that digitalization raises operational efficiency, customer engagement, the calibre of decision-making, and market access, all of which bolster business performance (Kraus. et al., 2021).

Still, digital transformation amounts to much more than merely acquiring new technology. It demands a rethinking of business models and of the organizational competencies that let firms cope effectively with environmental uncertainty (Warner & Wäger, 2019). Turning digital can shore up organizational resilience, encourage the reinvention of business models, and strengthen how customer value is created (Bouwman et al., 2020; Matarazzo et al., 2021; Priyono et al., 2020). Firms that build data-driven cultures, in much the same way, are inclined to lift their innovation and adaptability (Chatterjee et al., 2021). Nonetheless, whether digital transformation delivers returns rests on a firm's ability to render digital competencies into strategic advantages capable of sustaining it over time (Nadkarni & Prügl, 2021).

Yet another decisive factor behind SME sustainability is product innovation. The notion encompasses bringing out fresh offerings or substantially improving current ones with respect to design, functionality, quality, and the value customers receive (OECD/Eurostat, 2018). By way of innovation, firms are able to track shifting consumer preferences, distinguish themselves from competitors, and put forward more compelling value propositions (Garcia & Calantone, 2002). Innovation matters all the more for SMEs anchored in local wisdom, given that it allows long-established products to retain their


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relevance in present-day markets while their cultural authenticity is preserved. Earlier studies have shown that product innovation feeds positively into competitiveness, organizational performance, and business sustainability by sustaining continuous value creation and quick responses to market movement (Hanaysha et al., 2022; Makhloufi et al., 2021).

Why SMEs rooted in local wisdom matter strategically is best grasped through the Resource-Based View (RBV), which posits that durable competitive advantage arises from resources that are valuable, uncommon, tough to imitate, and woven into the organization (Barney, 1991; Wernerfelt, 1984). Under this framing, cultural heritage, passed-down know-how, artisanal skills, and local identities act as singular intangible assets that competitors are unable to copy with ease. Such assets create room for differentiation and lasting competitiveness. Earlier scholarship has underlined that scarce resources, the capacity to innovate, and distinctive value propositions contribute markedly to the competitiveness and sustainability of SMEs (Ceptureanu et al., 2020; Ferasso et al., 2020; Vecchio et al., 2021).

While RBV speaks to the strategic value held in resources, Dynamic Capabilities Theory places emphasis on a firm's ability to assemble, grow, and rework those resources as circumstances change (Teece et al., 1997). According to Teece (2018), firms hold on to competitiveness by sensing opportunities, taking hold of them, and refashioning their resources to suit. Looked at in this light, digitalization and product innovation function as dynamic capabilities through which local wisdom-based SMEs turn cultural endowments into durable market value. By adjusting technologically and innovating continually, these enterprises can sharpen differentiation, customer engagement, and resilience.

Even though academic interest in digitalization and innovation has been mounting, several gaps are still open. For one, the bulk of earlier studies have fixed on how these factors bear directly on performance, while the routes through which they mould long-run sustainability have received comparatively little scrutiny (Amankwah-Amoah et al., 2021; Nadkarni & Prügl, 2021). On top of that, the empirical record on how digitalization and innovation influence sustainability remains inconclusive, hinting that mediating factors may be at play. Beyond this, work focused on local wisdom-based SMEs stays rather thin, particularly in developing-country settings where cultural endowments serve as principal fountains of competitive differentiation (Ferasso et al., 2020; Matarazzo et al., 2021).

To bridge these gaps, this study casts competitive advantage as the mediating tie binding digitalization and product innovation to SME sustainability. Competitive


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advantage denotes a firm's ability to furnish superior value through differentiation, quality, reputation, and the allegiance of its customers (Porter, 1985). Read through the RBV lens, competitive advantage emerges as the result of deploying strategic resources to good effect (Barney, 1991). It follows that digitalization and product innovation are expected to bolster sustainability both directly and, in a roundabout way, by spawning enduring competitive advantages.

The contribution of this study to the literature is threefold. To begin, it widens RBV by demonstrating how local wisdom serves as a strategic intangible asset that digitalization and product innovation are able to strengthen. Next, it enriches Dynamic Capabilities Theory by laying out how SMEs convert cultural resources into durable market value through technological adjustment and innovation. Finally, it furnishes empirical support for the mediating part competitive advantage plays in explaining the connections among digitalization, product innovation, and sustainability.

On that basis, the study undertakes to gauge how digitalization and product innovation bear on the durability of locally rooted SMEs in Banjarmasin and to examine the mediating role that competitive advantage assumes across those connections. By zeroing in on culturally embedded firms, it seeks to reveal how inherited resources can be reworked into sustainable competitive advantages in the digital era.

## METHOD

### Research Design and Sample

Adopting a quantitative, explanatory design, this study set out to examine how digitalization, product innovation, competitive advantage, and sustainability interconnect within locally rooted SMEs The fieldwork was carried out among such firms operating in Banjarmasin, South Kalimantan, Indonesia, taking in producers of Sasirangan textiles, traditional food sellers, handicraft makers, and herbal-product manufacturers.

Data were collected with a structured questionnaire distributed to the proprietors and managers of these SMEs. By means of purposive sampling, respondents were picked on the basis of how involved they were in operating the business, in innovation work, and in adopting digital technology. From the 220 questionnaires sent out, 200 were returned and deemed usable, which yields a response rate of 90.9%. That respondent count comfortably clears the minimum that PLS-SEM requires (Hair et al., 2021).


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**Measurement of Variables**

Each construct was measured with indicators drawn from earlier validated work and tweaked to fit the circumstances of local wisdom-based SMEs. Their answers were registered on a Likert scale of five points, where 1 stood for strong disagreement and 5 for strong agreement.

Digitalization was captured by items reflecting the extent to which digital technologies were taken up and used across operations, marketing, customer dealings, and information handling. Product Innovation was measured through the development of products, improvements to design, the differentiation of products, and the firm's readiness to respond to market change. Competitive Advantage took in product distinctiveness, superior quality, differentiation, and the generation of value for customers. SME Sustainability was assessed with items linked to continuity of the business, adaptability, prospects for growth, and the firm's viability over the long term.

**Data Analysis**

The data were analysed in SmartPLS 4.0 by means of PLS-SEM (Hair et al., 2021; Sarstedt et al., 2022). The analysis proceeded across two stages: first the measurement model was appraised, and then the structural model.

Three checks underpinned the assessment of the measurement model: reliability, convergent validity, and discriminant validity. Convergent validity was read from the outer loadings together with the Average Variance Extracted (AVE); discriminant validity rested on the Heterotrait–Monotrait Ratio, or HTMT (Henseler et al., 2015). Reliability, for its part, was verified using Cronbach's alpha together with Composite Reliability.

The structural model was examined in terms of path coefficients, effect sizes ($f^2$), predictive relevance ($Q^2$), the coefficient of determination ($R^2$), and the testing of the hypotheses. To gauge significance, a bootstrapping procedure that drew 5,000 subsamples was run. Mediation was assessed via indirect-effect analysis paired with the Variance Accounted For (VAF) technique in line with Hayes (2022). To close, an Importance–Performance Matrix Analysis (IPMA) was undertaken to single out the managerial priorities with the greatest promise for lifting SME sustainability.



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## RESULT

### Respondent Characteristics

In all, 220 questionnaires went to the owners and managers of local wisdom-based SMEs across Banjarmasin, South Kalimantan. From these, 200 were sent back and regarded as fit for analysis, which gives a response rate of 90.9%.

A look at the respondent profile reveals that women made up 58% and men 42%. The bulk sat in the 31-to-40 age band (43%), with the 41-to-50 group next (31%). On schooling, the biggest portion had completed senior secondary or vocational study (46%), whereas 38% held a bachelor's degree.

Turning to the firms, 52% were run by families. The majority had traded for 6–10 years (41%), trailed by those operating 2–5 years (35%) and those past the 10-year mark (24%). The businesses covered an assortment of local wisdom-based sectors: Banjar traditional cakes (28%), Sasirangan textiles (22%), Purun woven products (18%), traditional herbal goods (12%), batik and textile products (12%), and metal handicrafts (8%).

**Table 1. Profile of Respondents and Their Businesses**

| Category | Description | Percentage (%) |
|---|---|---|
| Gender | Female | 58 |
| | Male | 42 |
| Age | 31–40 years | 43 |
| | 41–50 years | 31 |
| Education | High School/Vocational | 46 |
| | Bachelor's Degree | 38 |
| Business Ownership | Family-Owned | 52 |
| Business Age | 2–5 years | 35 |
| | 6–10 years | 41 |
| | >10 years | 24 |
| Business Sector | Traditional Cakes | 28 |
| | Sasirangan Textiles | 22 |
| | Purun Weaving | 18 |
| | Herbal Products | 12 |
| | Batik/Textiles | 12 |
| | Metal Handicrafts | 8 |



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**Measurement Model Assessment**

Scrutiny of the measurement model turned on convergent validity, discriminant validity, and reliability. The findings show that each construct cleared the advised benchmarks.

Where convergent validity is concerned, the outer-loading figures and the AVE were inspected. Each indicator returned a loading above the suggested floor of 0.708, falling somewhere between 0.743 and 0.891. Beyond that, every AVE reading topped 0.50, which signals that the constructs captured more than half of the variance in their indicators (Hair et al., 2021).

**Table 2. Results for Convergent Validity**

| Construct | Outer Loading Range | AVE |
|---|---|---|
| Digitalization | 0.743–0.834 | 0.648 |
| Product Innovation | 0.778–0.865 | 0.672 |
| Competitive Advantage | 0.801–0.891 | 0.711 |
| SME Sustainability | 0.769–0.856 | 0.693 |

Discriminant validity, in turn, drew on the HTMT. As set out in Table 3, the HTMT readings all lay between 0.652 and 0.788, comfortably under the 0.85 limit that is usually advised. These figures confirm that the constructs stand empirically apart from one another.

**Table 3. HTMT Discriminant Validity**

| Constructs | DIG | INO | CA | SUS |
|---|---|---|---|---|
| Digitalization (DIG) | - | | | |
| Product Innovation (INO) | 0.652 | - | | |
| Competitive Advantage (CA) | 0.721 | 0.698 | - | |
| SME Sustainability (SUS) | 0.743 | 0.712 | 0.788 | - |

Reliability was gauged using Cronbach's Alpha and Composite Reliability (CR). Each construct yielded values past the advised floor of 0.70, which points to sound internal consistency and dependability.

**Table 4. Reliability Outcomes**

| Construct | Cronbach's Alpha | Composite Reliability |
|---|---|---|
| Digitalization | 0.865 | 0.903 |



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| | | |
|---|---|---|
| Product Innovation | 0.878 | 0.911 |
| Competitive Advantage | 0.919 | 0.936 |
| SME Sustainability | 0.927 | 0.941 |

**Structural Model Assessment**

The explanatory strength of the structural model was judged via predictive relevance ($Q^2$) and the coefficient of determination ($R^2$). The results indicate that Digitalization and Product Innovation, in combination, capture 64.7% of the variation in Competitive Advantage ($R^2 = 0.647$). Adding Competitive Advantage to the two, the trio jointly accounts for 73.2% of the variation in SME Sustainability ($R^2 = 0.732$).

The $Q^2$ readings for Competitive Advantage (0.451) and SME Sustainability (0.498) both sit above zero, which denotes acceptable predictive relevance by the Stone–Geisser benchmark.

**Table 5. Evaluation of the Structural Model**

| Endogenous Construct | $R^2$ | Adjusted $R^2$ | $Q^2$ |
|---|---|---|---|
| Competitive Advantage | 0.647 | 0.643 | 0.451 |
| SME Sustainability | 0.732 | 0.727 | 0.498 |

**Hypothesis Testing**

The hypotheses were assessed using a bootstrapping procedure that drew on 5,000 subsamples. The findings indicate that each of the proposed direct links is statistically significant.

**Table 6. Results of Direct Effects**

| Hypothesis | Relationship | β | t-value | p-value | $f^2$ | Result |
|---|---|---|---|---|---|---|
| H1 | Digitalization → Competitive Advantage | 0.412 | 6.874 | <0.001 | 0.187 | Supported |
| H2 | Product Innovation → Competitive Advantage | 0.438 | 7.329 | <0.001 | 0.211 | Supported |
| H3 | Competitive Advantage → Sustainability | 0.523 | 9.156 | <0.001 | 0.342 | Supported |
| H4 | Digitalization → Sustainability | 0.265 | 4.721 | <0.001 | 0.089 | Supported |


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| | | | | | | |
|---|---|---|---|---|---|---|
| H5 | Product Innovation → Sustainability | 0.187 | 3.234 | 0.001 | 0.044 | Supported |

The results indicate that Digitalization bears significantly on Competitive Advantage (β = 0.412, p < 0.001), which supports H1. Product Innovation, too, delivers a significant positive effect on Competitive Advantage (β = 0.438, p < 0.001), upholding H2. Competitive Advantage then significantly conditions SME Sustainability (β = 0.523, p < 0.001), validating H3.

On top of that, Digitalization and Product Innovation each show significant positive effects on SME Sustainability, which backs H4 and H5.

**Mediation Analysis**

The mediating part of Competitive Advantage was investigated by way of indirect-effect analysis paired with the Variance Accounted For (VAF) measure. The findings indicate meaningful indirect effects on both mediation paths.

**Table 7. Outcomes of the Mediation Analysis**

| Hypothesis | Indirect Relationship | Indirect Effect | t-value | p-value | VAF (%) | Mediation Type |
|---|---|---|---|---|---|---|
| H6 | Digitalization → Competitive Advantage → Sustainability | 0.216 | 5.892 | <0.001 | 44.9 | Partial |
| H7 | Product Innovation → Competitive Advantage → Sustainability | 0.229 | 6.124 | <0.001 | 55.0 | Partial |

The results indicate that Competitive Advantage conveys part of the connection between Digitalization and SME Sustainability, mirrored in a VAF of 44.9%. By the same token, it partly carries the tie between Product Innovation and SME Sustainability, with a VAF of 55.0%. H6 and H7 are accordingly supported.


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**Importance–Performance Matrix Analysis (IPMA)**

To pin down the managerial priorities best suited to lifting SME Sustainability, an IPMA was run. It places Competitive Advantage at the top on importance (0.523), with Digitalization (0.481) and Product Innovation (0.416) following.

**Table 8. IPMA Outcomes**

| Construct | Importance | Performance | Gap |
|---|---|---|---|
| Competitive Advantage | 0.523 | 3.89 | 1.11 |
| Digitalization | 0.481 | 3.72 | 1.28 |
| Product Innovation | 0.416 | 3.94 | 1.06 |

Among the trio of constructs, Digitalization shows the broadest distance between its importance and its performance. This suggests that strengthening digital capabilities is the managerial step with the greatest promise for raising the sustainability of local wisdom-based SMEs.

## DISCUSSION

The results of this study lend firm empirical weight to the proposition that digitalization, product innovation, and competitive advantage are consequential drivers of sustainability for local wisdom-based SMEs. All of the proposed hypotheses hold, and the analysis verifies that competitive advantage functions as the strategic channel by which digitalization and innovation nourish long-term sustainability.

The first result establishes that digitalization works in favour of competitive advantage. This points to digitally equipped SMEs being better situated to firm up their market presence, lift customer engagement, and mark themselves out from competitors. Where local wisdom-based SMEs are concerned, digital means make it easier to carry culturally grounded products to wider audiences while geographic constraints recede. Through channels such as social media, e-commerce applications, online communication, and facilities for digital payment, these firms can raise their visibility and grow easier for customers to reach.

This finding chimes with Dynamic Capabilities Theory, which holds that firms must go on adapting and reorganizing their resources to keep up with shifts in the environment (Teece, 2018; Teece et al., 1997). Digitalization equips firms to spot market openings, seize fresh demand, and remould customary practices into more competitive business


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models. The result tallies with prior studies showing that digital transformation lifts organizational competitiveness by improving responsiveness, operational efficiency, and the creation of customer value (S.kraus et al., 2021; Verhoef et al., 2021)

Beyond that, the result bolsters the contention that digital transformation ought to be viewed not as simply acquiring technology but as a strategic act of organizational renewal (Warner & Wäger, 2019). SMEs that successfully fold digital technologies into their business models are likelier to forge sustainable competitive footholds (Matarazzo et al., 2021). Along the same lines, organizations that draw on data-driven decision-making tend to reach greater innovation and performance, which fortifies their competitive standing (Chatterjee et al., 2022).

The second result shows that product innovation appreciably strengthens competitive advantage. It signals that innovation stays a crucial route to firming up competitiveness among local wisdom-based SMEs. By means of product innovation, firms are able to introduce fresh features, raise quality, modernize design, and fit traditional goods to changing consumer preferences while their cultural authenticity stays intact.

Viewed from the Resource-Based View, innovation lifts the value of a firm's resources by yielding distinctive offerings that competitors find hard to mimic (Barney, 1991; Wernerfelt, 1984). In enterprises anchored in local wisdom, handed-down knowledge and cultural heritage make up valuable strategic assets. Innovation is able to reshape these assets into present-day products that hold on to cultural meaning while gaining wider market appeal. The result accords with earlier research suggesting that innovation contributes in a constructive way to competitive positioning, organizational learning, the generation of customer value, and differentiation (Garcia & Calantone, 2002; Hanaysha et al., 2022; Makhloufi et al., 2021) The results go on to reveal that competitive advantage wields the strongest direct effect on SME sustainability. This bears out that sustainability leans heavily on a firm's ability to provide greater value than competitors by way of product distinctiveness, steady quality, reputation, and customer loyalty. Competitive advantage registered the largest effect size of every relationship examined, which highlights its central role in keeping business performance going.

This result fits well with the Resource-Based View, which holds that sustainable performance grows out of the effective use of resources that are valuable, uncommon, and difficult to copy (Barney, 1991). Franco and Haase (2015) likewise underline that a firm's resources and core competencies make up the foundation of enduring competitive advantage and long-run performance. Among such locally grounded SMEs, traditional


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craftsmanship and cultural identity supply singular sources of differentiation that shore up the durability of the business.

The direct effects that digitalization and product innovation exert on sustainability likewise came out significant. This indicates that digital competencies and innovation work flow straight into business continuity, adaptability, and sustained growth. Digital technologies allow SMEs to operate more efficiently, trim transaction costs, extend their market reach, and respond more deftly to changing customer expectations. Product innovation, for its part, lets firms go on producing value and stay relevant in turbulent market conditions.

The positive link between digitalization and sustainability takes on particular meaning in the post-pandemic commercial climate. Recent work observes that the COVID-19 crisis sped up digital transformation across industries and brought into focus how essential digital capabilities are for organizational resilience (Amankwah-Amoah et al., 2021). Similarly, Priyono et al. (2020) noted that digital transformation proved decisive in helping SMEs rework their business models during uncertain times. Digitalization, then, can be regarded as a key strategic investment that raises both competitiveness and sustainability.

Another significant contribution of this work is its pinpointing of competitive advantage as the mediating mechanism. That mediation analysis indicated that competitive advantage conveys part of both the digitalization–sustainability tie and the product innovation–sustainability tie. The VAF figures show that a considerable portion of the impact of digitalization and innovation on sustainability runs through the formation of competitive advantage.

These results bring meaningful theoretical implications. To start, they suggest that digitalization and innovation by themselves are not enough to guarantee sustainability. Rather, such capabilities need to be turned into competitive advantages that produce superior customer value and differentiation. This goes some way toward explaining why earlier studies have yielded inconsistent findings on the bearing of digitalization and innovation on organizational performance and sustainability (Nadkarni & Prügl, 2021).

Next, the evidence lends weight to bringing together the Resource-Based View and Dynamic Capabilities Theory. RBV accounts for the strategic value of local cultural resources, whereas Dynamic Capabilities Theory accounts for how firms put digitalization and innovation to work in turning those resources into durable market advantages. In combination, the two perspectives deliver a more rounded explanation of sustainability among local wisdom-based SMEs.


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The IPMA findings offer added managerial insight. Although product innovation posts the strongest performance of the constructs examined, digitalization carries the broadest distance between importance and performance. This indicates that digital capabilities remain underbuilt in spite of their sizable contribution to sustainability. Accordingly, spending on digital infrastructure, digital marketing, the adoption of e-commerce, and the building of digital skills should figure among the strategic priorities of SME owners and policymakers.

The results carry weight for sustainable development too. Echoing what the Triple Bottom Line framework holds (Elkington, 1997), sustainability for local wisdom-based SMEs extends past economic returns to take in the safeguarding of cultural heritage and community welfare. By drawing on digitalization and innovation, these firms can keep local traditions alive while securing durable economic viability at the same time.

On the whole, this study demonstrates that how well locally rooted SMEs endure is not settled by the holding of distinctive cultural resources alone. Rather, it turns on whether a firm can transmute its cultural resources into competitive advantages through digital and innovative effort. Capabilities of this kind let SMEs hold on to cultural authenticity, sharpen their competitive edge, and achieve sustainable growth in markets that keep growing more dynamic and technology-driven.

## THEORETICAL AND PRACTICAL IMPLICATIONS

This research contributes several worthwhile additions to the body of work on strategic management, innovation, digital transformation, and the sustainability of SMEs. First, the findings lend fresh support to the Resource-Based View (RBV): handled and nurtured properly, local wisdom emerges as a valuable strategic resource able to generate sustainable competitive advantage (Barney, 1991; Wernerfelt, 1984). The evidence shows that cultural heritage, handed-down knowledge, artisanal skills, and local identity make up intangible assets that competitors struggle to replicate. By themselves, though, these resources cannot secure long-run sustainability unless complementary organizational capabilities stand behind them.

Second, the work pushes Dynamic Capabilities Theory further by showing that digitalization and product innovation operate as strategic capabilities through which firms turn cultural resources into durable market value (Teece, 2018; Teece et al., 1997). The pronounced effects of digitalization and product innovation on competitive advantage establish that firms must keep adapting, integrating, and rearranging resources to remain competitive amid rapidly shifting business conditions. This is in line with earlier studies


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underscoring that digital transformation is better understood as organizational renewal in process rather than as merely adopting technology (Matarazzo et al., 2021; Warner & Wäger, 2019).

Third, the study enriches the growing sustainability literature by making plain the mechanism whereby organizational capabilities mould sustainable business outcomes. The notable mediating role of competitive advantage shows that digitalization and product innovation serve sustainability not solely in a direct manner but also indirectly, by producing greater customer value and sharper market differentiation. This addresses a significant gap left by prior studies that centred chiefly on the direct connections among these variables (Amankwah-Amoah et al., 2021; Nadkarni & Prügl, 2021).

On the practical front, the findings hold important lessons for SME owners, managers, and policymakers. They show that competitive advantage stands as the strongest predictor of sustainability. Owners should thus place priority on strategies that bolster customer loyalty, brand reputation, consistent quality, product distinctiveness, and differentiation. These factors are vital for sustaining competitiveness over the long term and for keeping the business going.

The findings further single out digitalization as an area deserving sharper managerial attention. The IPMA output shows it carrying the broadest distance between importance and performance, which signals considerable potential left untapped. Owners should therefore direct resources toward e-commerce platforms, online marketing, systems for managing customer relationships, digital payment facilities, and analytics capabilities. Such investment is expected to raise operational efficiency, extend market reach, and strengthen customer engagement (Kraus. et al., 2021; Verhoef et al., 2021).

Where policymakers are concerned, the findings highlight the value of bolstering the digital ecosystems on which locally rooted SMEs depend. Public programmes should target not only the conservation of cultural heritage but also the lifting of technological readiness through the build-out of digital infrastructure, the running of training schemes, support for innovation, and the provision of financial aid. Earlier research has shown that digital transformation strengthens organizational resilience and adaptability, above all when the environment grows uncertain (Jie et al., 2020; Priyono et al., 2020).

On top of this, SMEs should keep pursuing product innovation while preserving their cultural authenticity. Innovation strategies should set out to modernize traditional goods and raise their market relevance without giving up local identity. By coupling cultural distinctiveness with technological adjustment and innovation, local wisdom-based


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SMEs can attain sustainable growth and, in the same stroke, protect valuable cultural assets for the generations ahead.

## CONCLUSION

This study set out to examine how digitalization and product innovation bear on how well locally rooted SMEs endure, with competitive advantage taken as the variable doing the mediating. Its findings establish that digitalization and product innovation appreciably raise competitive advantage, which then emerges as the leading determinant of SME sustainability. Digitalization and innovation also act directly on sustainability, while competitive advantage carries part of these connections.

The study brings out that how well local wisdom-based SMEs endure turns not only on the possession of distinctive cultural resources but also on the capacity to recast them into competitive advantages through digitalization and relentless innovation. These results stress how central organizational capabilities are to constructing long-term business resilience and growth.

In practical terms, SME owners should put approaches that bolster differentiation and customer value, alongside product innovation and the take-up of digital tools, at the head of their agenda. Policymakers, meanwhile, are encouraged to back SMEs by building digital infrastructure, providing training programmes, and rolling out innovation-oriented schemes that raise competitiveness and sustainability.

A limitation of this study rests in its focus on one geographic area and in its cross-sectional design. Future work could broaden the geographic reach, take up longitudinal approaches, and incorporate further variables, among them government support, the maturity of digital capability, organizational resilience, and entrepreneurial orientation. All told, sustainable growth among local wisdom-based SMEs can be attained by uniting cultural resources with the capabilities of digital transformation and innovation.

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