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Digital Financial Literacy and Usage as Determinants of SME Financial Performance: Evidence from Kurunegala District, Sri Lanka

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ABSTRACT

Small and medium-sized enterprises (SMEs) increasingly rely on digital financial technologies to improve business operations and financial management. However, limited empirical evidence exists regarding how digital financial literacy and digital financial usage jointly influence SME financial performance in Sri Lanka, particularly at the district level. Despite growing interest in digital financial inclusion, limited empirical studies have examined this combined effect in district-level Sri Lankan contexts. Therefore, this study examines the impact of digital financial literacy and digital financial usage on the financial performance of SMEs in the Kurunegala District, Sri Lanka. A quantitative cross-sectional research design was adopted, and primary data were collected through a structured questionnaire from 64 SME owners and managers using convenience sampling. Descriptive statistics, correlation analysis, and multiple regression analysis were conducted using JAMOVI software. The findings reveal that both digital financial literacy and digital financial usage have a significant positive effect on SME financial performance. The regression model explained 62.1% of the variance in financial performance, with digital financial literacy demonstrating a stronger association than digital financial usage. This study contributes to limited Sri Lankan literature by providing district-level evidence from Kurunegala on digital financial capabilities and SME performance. However, findings are constrained by a small sample size (n=64) and convenience sampling, limiting generalizability. The study offers practical implications for policymakers and financial institutions in strengthening SME digital financial capabilities.

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1. Introduction

Small and medium-sized enterprises (SMEs) represent a fundamental pillar of economic development in Sri Lanka, contributing significantly to employment generation, income distribution, and regional economic development. In semi-urban and developing districts such as Kurunegala, SMEs serve as key drivers of local economic activity and entrepreneurship. Despite their importance, many SMEs face persistent challenges in maintaining sustainable financial performance due to limited access to financial resources, inadequate financial management practices, and low adoption of modern financial technologies.

The rapid advancement of digital technologies has significantly transformed the global financial landscape. In Sri Lanka, the increasing availability of online banking platforms, mobile payment systems, digital accounting software, and other electronic financial services has reshaped how businesses manage financial transactions. These digital financial tools offer opportunities to improve efficiency, transparency, and financial decision-making. However, these benefits can only be fully realized when SME owners and managers possess the necessary knowledge and skills to utilize such technologies effectively.

Digital financial literacy refers to the knowledge and skills required to understand and effectively operate digital financial tools. In addition to literacy, the effective usage of digital financial services plays a crucial role in determining SME business outcomes. For SMEs, digital financial literacy and digital financial usage represent distinct but complementary capabilities that jointly influence SME financial outcomes, including financial planning, budgeting, cash flow management, and overall business sustainability. In the Sri Lankan context, prior studies have examined the role of financial literacy and digital financial services in improving SME performance (Weerakoon & Anuradha, 2023). Furthermore, limited district-level empirical evidence exists regarding the combined influence of digital financial literacy and digital financial usage on SME financial performance within the Sri Lankan context, particularly in emerging SME regions such as Kurunegala.

Unlike prior studies conducted at national or multi-regional levels, this study focuses on Kurunegala District, an emerging SME hub where digital financial adoption remains uneven and under-researched. By jointly examining digital financial literacy and digital financial usage, this study provides localized empirical evidence on how digital financial capabilities translate into SME financial performance in a semi-urban Sri Lankan context, thereby extending existing national-level findings. To the author's knowledge, very limited empirical studies have jointly examined digital financial literacy and digital financial usage within a district-level SME context in Sri Lanka.

Despite increasing digital financial transformation in Sri Lanka, limited empirical evidence exists on the combined effect of digital financial literacy and digital financial usage on SME financial performance at the district level. In particular, Kurunegala District remains under-researched despite its growing SME base and increasing exposure to digital financial systems, creating a clear need for context-specific empirical investigation. Therefore, this study addresses the following research questions:

1. Does digital financial literacy significantly influence SME financial performance?
2. Does digital financial usage significantly influence SME financial performance?
3. Which factor has a stronger influence on SME financial performance?

This study aims to examine the impact of digital financial literacy and digital financial usage on the financial performance of SMEs in the Kurunegala District, Sri Lanka. A quantitative cross-sectional research approach was employed to analyse the relationships between these variables and SME financial performance.

The findings of this study contribute to both academic literature and practical policy development. Specifically, the study provides empirical evidence to support the design of targeted training programs, institutional support mechanisms, and policy initiatives aimed at enhancing digital financial capabilities among SME operators. Strengthening these capabilities can serve as a strategic pathway to improving SME sustainability and promoting long-term economic development in Sri Lanka.

2. Literature Review

2.1. Small and Medium-Sized Enterprises (SMEs) and Financial Performance

SMEs are widely recognized as key contributors to economic development, innovation, and employment generation. In Sri Lanka, SMEs account for a significant proportion of business establishments and provide substantial employment opportunities across multiple sectors including manufacturing, retail, agriculture, and services. However, SMEs often face challenges related to financial management, limited technological capabilities, restricted access to finance, and operational inefficiencies.

The increasing digitalization of financial services has created opportunities for SMEs to overcome some of these limitations. Through digital financial platforms, SMEs can improve transaction efficiency, financial planning, customer service, and operational performance. Consequently, the adoption of digital

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financial capabilities has become increasingly important for SME sustainability and competitiveness.

2.2. Digital Financial Literacy

Digital financial literacy refers to the ability to understand, evaluate, and effectively utilize digital financial products and services. It includes knowledge of online banking, mobile payment systems, digital security, financial applications, and digital financial decision-making.

Previous studies indicate that digital financial literacy positively influences financial behaviour and business performance. SME owners with higher levels of digital financial literacy are more likely to adopt digital financial tools, make informed financial decisions, manage risks effectively, and improve business efficiency. Studies conducted in developing economies further suggest that digital financial literacy enhances financial inclusion and business sustainability.

However, previous findings are not entirely consistent across contexts. While some studies emphasize the direct influence of digital financial literacy on financial performance, others argue that literacy alone may not guarantee improved outcomes unless supported by active utilization of digital financial services and appropriate technological infrastructure.

2.3. Digital Financial Usage

Digital financial usage refers to the practical application and frequency of using digital financial technologies and services within business operations. It includes activities such as online transactions, mobile banking, digital payments, electronic fund transfers, and digital financial management. The increasing use of digital financial services allows SMEs to improve operational efficiency, reduce transaction costs, enhance accessibility to financial services, and strengthen financial management practices. Previous studies have reported positive relationships between digital financial usage and business performance, particularly among SMEs operating in digitally evolving markets.

Nevertheless, several studies also highlight that the effectiveness of digital financial usage depends on users' digital competencies and their ability to strategically integrate digital tools into business activities. Therefore, the relationship between digital financial usage and financial performance may vary depending on the level of digital financial literacy possessed by SME owners and managers.

2.4. Financial performance

Financial performance refers to the ability of a business to generate profitability, maintain liquidity, improve revenue growth, and achieve operational efficiency. For SMEs, financial performance is often measured using indicators such as sales growth, profitability, cash flow stability, and return on investment. Digital financial capabilities can improve SME financial performance by supporting efficient financial transactions, improving access to financial information, enhancing customer convenience, and reducing operational costs. Therefore, digital financial literacy and digital financial usage are increasingly viewed as important strategic resources influencing SME competitiveness and long-term sustainability.

2.5. Theoretical Foundation

Resource-Based View (RBV)

The Resource-Based View (RBV) theory explains that organizations achieve competitive advantage through valuable, rare, and difficult-to-imitate resources and capabilities. Within the SME context, digital financial literacy can be considered a strategic intangible resource that enables firms to improve decision-making, financial management, and operational efficiency.

According to RBV, SMEs possessing strong digital financial capabilities are better positioned to utilize financial technologies effectively and achieve superior business performance compared to competitors lacking such capabilities.

Technology Acceptance Model (TAM)

The Technology Acceptance Model (TAM) explains how users adopt and utilize technology based on perceived usefulness and perceived ease of use. In the context of SMEs, digital financial usage is influenced by business owners' perceptions regarding the benefits, efficiency, and convenience of digital financial technologies.

TAM supports the argument that SME owners and managers are more likely to adopt digital financial technologies when they perceive such technologies as useful, accessible, and beneficial for improving business performance.

2.6. Empirical Review and Research Gap

Previous empirical studies generally report a positive relationship between digital financial capabilities and SME performance; however, findings vary across contexts and dimensions of digital finance adoption. While some studies emphasize the importance of digital financial literacy as a strategic capability influencing profitability and operational efficiency, others suggest that literacy alone may not produce improved business performance unless SMEs actively utilize digital financial tools in business operations.

Although previous international studies have examined digital financial literacy, digital finance adoption, and SME performance, several gaps remain. First, many studies examine digital literacy and digital usage separately rather than jointly. Second, limited empirical evidence exists within the Sri Lankan SME context, particularly at the district level. Third, few studies

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integrate both RBV and TAM to explain how digital financial capabilities influence SME financial performance.

Therefore, this study attempts to address these gaps by examining the combined effects of digital financial literacy and digital financial usage on SME financial performance in the Kurunegala District, Sri Lanka

2.7. Hypotheses Development

Based on the literature and theoretical foundation, the following hypotheses were developed:

H1: Digital financial literacy has a significant positive impact on SME financial performance.

H2: Digital financial usage has a significant positive impact on SME financial performance.

2.8. Conceptual Framework

Conceptual Model Development

This study is grounded in the Resource-Based View (RBV) and the Technology Acceptance Model (TAM) developed by Davis (1989). TAM explains how perceived usefulness and perceived ease of use influence technology adoption, particularly in the context of digital financial tools, ultimately enhancing SME performance (Thathsarani & Jianguo, 2022).

This study conceptualizes digital financial capabilities as key determinants of SME financial performance. RBV suggests that intangible resources such as knowledge and skills enhance competitive advantage, while TAM explains how technology adoption influences usage behavior.

The study examines these digital financial capabilities through two main constructs:

Independent Variables (IVs):

- Digital Financial Literacy (DFL)
- Digital Financial Usage (DFU)

Dependent Variable (DV):

- Financial Performance of SMEs (FP)

Digital financial literacy reflects the knowledge and skills required to effectively understand and operate digital financial tools. In contrast, digital financial usage represents the actual adoption and use of these tools in business activities.

In this study, financial performance is assessed as a composite construct, incorporating key indicators such as profitability, revenue growth, and cash flow management. Prior studies confirm that digital adoption and literacy jointly influence business outcomes (Al Awadhi et al., 2024; Chinomona et al., 2025).

The conceptual framework proposes that higher levels of digital financial literacy and increased usage of digital financial tools lead to improved financial performance among SMEs. Furthermore, while digital financial literacy may support the effective use of digital financial tools, this study treats digital financial literacy and digital financial usage as independent but complementary determinants of financial performance.

Conceptual Framework Diagram

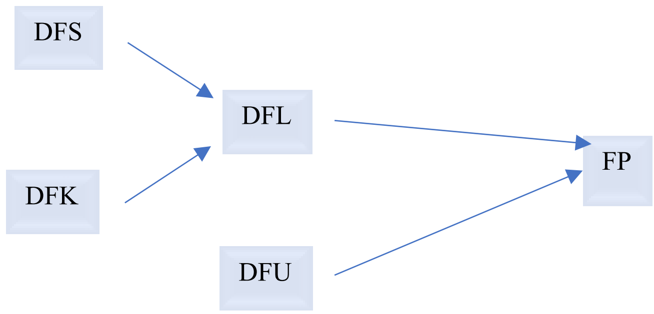

Figure 1: Conceptual Framework of Digital Financial Literacy and SME Financial Performance

- DFL is operationalized using two dimensions: digital financial knowledge and digital financial skills.
- FP is measured using profitability, revenue growth, and cash flow.

2.9. Explanation of the Framework

The conceptual framework of this study is based on the premise that both digital financial literacy and digital financial usage play critical roles in influencing the financial performance of SMEs. Digital financial literacy, which comprises digital financial knowledge and skills, enables SME owners and managers to make informed financial decisions, engage in effective financial planning, and manage business finances more efficiently.

Digital financial usage reflects the actual adoption and consistent use of digital financial platforms such as online banking, mobile payments, and digital accounting systems in day-to-day business operations. The active use of these tools enhances transaction efficiency, improves record-keeping accuracy, and supports better cash flow management. The framework assumes that SMEs with higher levels of digital financial literacy are more likely to utilize digital financial services effectively. Both digital financial literacy and digital financial usage are expected to positively influence financial performance, including profitability, revenue growth, and liquidity management.

Thus, digital financial literacy represents a capability resource, while digital financial usage reflects actual behavioural adoption of digital financial tools.

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3. Methodology

3.1. Research Design

This study adopts a quantitative research approach to examine the relationship between digital financial literacy, digital financial usage, and SME financial performance in the Kurunegala District, Sri Lanka. The survey questionnaire used for data collection is provided in Appendix A. A quantitative design was selected as the study aimed to test predefined hypotheses and examine statistical relationships among variables using numerical data. A cross-sectional design was employed, where data were collected at a single point in time from SME owners and managers operating in various industries within the district.

3.2. Population and Sampling

The target population comprised SME owners and managers operating in the Kurunegala District across sectors including retail, manufacturing, services, and trading. A sample of 64 SMEs was selected using a non-probability convenience sampling technique. Given the absence of a complete sampling frame for SMEs in the district and time constraints, convenience sampling was adopted to obtain primary data within accessibility limitations. This approach enables coverage of SMEs across key sectors in the district, although it limits generalizability. However, it is commonly applied in exploratory SME studies where comprehensive population lists are not available.

3.3. Data Collection Methods

The questionnaire consists of four sections:

1. Demographic information (business type, years of operation, number of employees, etc.)
2. Digital Financial Literacy
3. Digital Financial Usage
4. Financial Performance Indicators

Respondents evaluated all items using a five-point Likert scale:

1 = Strongly Disagree 2 = Disagree
3 = Neutral 4 = Agree
5 = Strongly Agree

The Likert scale was used to capture respondents' perceptions of digital financial capabilities and financial performance. Where available, secondary financial records were used to support the validity of self-reported financial performance measures. Ethical considerations were followed by ensuring voluntary participation, confidentiality of responses, and use of data solely for academic purposes.

3.4. Measurement of Variables

Digital Financial Literacy (DFL) – a multidimensional construct composed of:

- Digital Financial Knowledge (DFK)
- Digital Financial Skills (DFS)

Digital Financial Usage (DFU) – a separate construct representing the behavioral adoption of digital financial tools.

Financial Performance (FP) – Financial performance was measured based on respondents' perceptions of profitability, revenue growth, and cash flow management relative to prior business periods:

- Profitability
- Revenue Growth
- Cash Flow Management

All constructs were measured using multiple Likert-scale statements adapted from previous validated studies (Weerakoon & Anuradha, 2023; Dewmini et al., 2023) to ensure content validity. Respondents evaluated their business performance relative to prior periods using a five-point Likert scale.

The questionnaire was adapted from previously validated instruments and slightly modified for the Sri Lankan SME context. A pilot test was conducted to ensure clarity and relevance of items.

3.5. Reliability and Validity

Internal consistency reliability of each construct was assessed using Cronbach's Alpha, with a threshold of 0.70 considered acceptable. Content validity was ensured through the adoption of measurement items from previously validated studies, which were adapted to the Sri Lankan SME context. Construct validity was evaluated through factor structure consistency to ensure that the indicators appropriately represented their respective latent variables. All statistical analyses were conducted at a 5% significance level.

3.6. Data Analysis

Data were analyzed using JAMOVI software. The following techniques were employed:

- Descriptive statistics to summarize respondent characteristics
- Reliability analysis using Cronbach's Alpha
- Pearson correlation analysis to examine relationships among variables
- Multiple linear regression analysis to test the study hypotheses and examine the impact of DFL and DFU on FP

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Prior to regression analysis, key assumptions including normality, linearity, homoscedasticity, and multicollinearity were tested. Normality was assessed using residual distribution patterns, while multicollinearity was evaluated using Variance Inflation Factor (VIF). Linearity and homoscedasticity were examined using scatterplots of standardized residuals, confirming the suitability of the regression model.

4. Results and Discussion

Normality of residuals was assessed using histogram and P–P plots, indicating an approximately normal distribution. Homoscedasticity was evaluated using scatterplots of standardized residuals, showing no clear pattern. Multicollinearity was tested using VIF values, all of which were below 5, confirming no multicollinearity issues.

Reliability Analysis

Reliability of all constructs was assessed at the dimension level before constructing the composite Digital Financial Literacy (DFL) variable. Cronbach's Alpha values indicate strong internal consistency:

- Digital Financial Knowledge (DFK): $\alpha = 0.831$
- Digital Financial Skills (DFS): $\alpha = 0.861$
- Digital Financial Usage (DFU): $\alpha = 0.866$
- Financial Performance (FP): $\alpha = 0.880$

All values exceed the recommended threshold of 0.70, confirming that the measurement scales are reliable and internally consistent.

4.1. Correlation Analysis

Pearson correlation analysis was conducted to examine the relationships among digital financial literacy, digital financial usage, and financial performance. The results indicate strong positive relationships among all variables.

Digital financial literacy is strongly and positively correlated with digital financial usage ($r = 0.801$, $p < 0.001$). Additionally, digital financial usage shows a strong positive relationship with financial performance ($r = 0.733$, $p < 0.001$). Similarly, digital financial literacy is strongly and positively associated with financial performance ($r = 0.760$, $p < 0.001$). All relationships are statistically significant.

- DFL and DFU: $r = 0.801$, $p < 0.001$
- DFU and FP: $r = 0.733$, $p < 0.001$
- DFL and FP: $r = 0.760$, $p < 0.001$

Although all correlation coefficients are below 0.85, suggesting no severe multicollinearity concerns, multicollinearity was further assessed using Variance Inflation Factor (VIF) values in the regression analysis

4.2. *Regression Analysis*

To further examine the predictive relationships among variables, multiple linear regression analysis was conducted to assess the impact of digital financial literacy and digital financial usage on financial performance.

Model Coefficients - FP

Predictor	Estimate	SE	t	p	Stand. Estimate ((β)
Intercept	0.937	0.324	2.89	0.005	-
DFU	0.307	0.116	2.65	0.010	0.349
DFL	0.499	0.137	3.65	<.001	0.480

Table 1: Regression Analysis

The overall model is statistically significant ($F(2,61) = 49.9$, $p < 0.001$), explaining 62.1% of the variance in financial performance ($R^2 = 0.621$).

Both digital financial literacy and digital financial usage positively and significantly predict financial performance. Digital financial literacy shows a stronger influence ($\beta = 0.480$) compared to digital financial usage ($\beta = 0.349$), indicating that knowledge and skills play a more dominant role in enhancing SME performance.

Variance Inflation Factor (VIF) values were below 5, confirming that multicollinearity is not a concern. The results support **H1** and **H2**, indicating that both digital financial literacy and digital financial usage have a significant positive effect on SME financial performance.

5. Discussion

The findings of this study provide strong empirical support for both the Resource-Based View (RBV) and the Technology Acceptance Model (TAM). From the RBV perspective, digital financial literacy comprising knowledge and skills functions as a valuable intangible resource that enhances SMEs' ability to manage financial activities effectively. This capability enables better financial decision-making, improved cost control, and enhanced profitability, ultimately leading to superior financial performance.

From the TAM perspective, the results indicate that the adoption and usage of digital financial tools significantly influence business performance. SMEs that actively utilize digital financial tools demonstrate improved transaction

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efficiency, better financial record-keeping, and stronger cash flow management.

Specifically:

- Digital Financial Knowledge (DFK) enables informed financial decision-making, reducing errors and improving profitability.
- Digital Financial Skills (DFS) enhance transaction efficiency and support effective financial management, contributing to revenue growth.
- Digital Financial Usage (DFU) improves cash flow management through accurate record-keeping and real-time financial tracking.

These findings highlight that access to digital financial tools alone is insufficient. SMEs must also possess the necessary literacy and skills to effectively utilize these tools in order to achieve meaningful performance improvements. The positive effects of digital financial literacy and usage on SME performance are consistent with prior empirical findings, which suggest that digital financial competencies enhance financial decision-making and operational efficiency (Olubiyi, Abiodun and Oyeniyi, 2022; Munyua and Mwaura, 2023).

The findings are consistent with prior studies reporting positive relationships between digital financial literacy, digital financial usage, and SME performance. However, the stronger effect of digital financial literacy compared to digital financial usage differs from some previous studies that emphasize usage as the dominant factor. This variation may be explained by the relatively lower digital maturity of SMEs in emerging districts, where knowledge and skills play a more foundational role than advanced usage behavior.

5.1. Implications of the Study

Theoretical Implications

This study makes a meaningful contribution to the literature on SME financial performance by emphasizing the role of digital financial literacy (DFL) and digital financial usage (DFU) as key determinants of business outcomes. While previous research has largely focused on traditional financial literacy, the role of digital competencies remains underexplored, particularly in emerging economies such as Sri Lanka, where SMEs play a vital role in economic development.

By integrating the Resource-Based View (RBV) and the Technology Acceptance Model (TAM), this study provides a comprehensive theoretical explanation of how digital financial capabilities influence firm performance. According to RBV, firm performance depends on valuable, rare, and inimitable resources that generate sustained competitive advantage (Barney, 1991). In this context, digital financial literacy can be considered an intangible strategic resource that enhances SMEs' ability to manage financial activities effectively.

At the same time, TAM explains how perceived usefulness and ease of use drive the adoption of digital technologies. In this study, digital financial usage represents the behavioural application of digital financial knowledge and skills. Together, these constructs explain variations in financial performance, highlighting the relationship between capability (literacy) and action (usage).

Furthermore, this research addresses an important empirical gap by providing district-level evidence from Kurunegala. The findings demonstrate that the value of intangible resources such as digital financial literacy is context-dependent, reinforcing the applicability of RBV and TAM in emerging market settings.

Managerial Implications

The findings of this study provide important insights for SME owners and managers. The results highlight that developing digital financial knowledge alone is insufficient; the effective application of digital financial tools is essential for improving financial decision-making and operational efficiency.

SME managers are encouraged to adopt and integrate digital financial platforms, such as online banking systems, mobile payment applications, and digital accounting software, into their daily business operations. The use of these tools can enhance budgeting accuracy, improve financial planning, and support more effective cash flow monitoring.

In addition, SMEs should promote the consistent use of digital financial tools within their organizations to ensure that the benefits of digital adoption are fully realized. Strengthening both digital financial literacy and usage enables SMEs to improve profitability, achieve sustainable growth, and enhance operational transparency.

Overall, digital financial literacy should be viewed as a strategic investment that supports long-term business sustainability rather than merely an operational tool.

Policy Implications

The findings of this study also have important implications for policymakers, financial institutions, and development agencies seeking to strengthen the SME sector. Targeted interventions can play a significant role in enhancing digital financial literacy and usage among SMEs. These may include structured training programs and workshops designed to build both theoretical knowledge and practical digital skills. In addition, mentoring and advisory services can support SMEs in the adoption and effective implementation of digital financial systems.

Collaboration between government agencies and financial institutions is also essential in creating an enabling environment that supports SME digital transformation. Such initiatives can

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improve access to digital financial services, enhance financial transparency, and promote innovation within the SME sector. Collectively, these measures can contribute to the development of a more resilient SME ecosystem, supporting sustainable economic growth at both regional and national levels.

6. Conclusion

This study examined the impact of digital financial literacy (DFL) and digital financial usage (DFU) on the financial performance of SMEs in the Kurunegala District, Sri Lanka. SMEs play a pivotal role in driving economic growth, employment generation, and regional development. Despite their importance, many SMEs face challenges in sustaining financial performance due to limited access to financial resources, inadequate management practices, and low adoption of modern financial technologies.

The findings indicate that both DFL and DFU positively and significantly influence financial performance. SMEs with higher levels of digital financial knowledge and skills, combined with effective usage of digital tools, are more likely to achieve enhanced profitability, revenue growth, and efficient cash flow management. These results highlight that knowledge and application must go hand in hand; access to digital tools alone does not automatically translate into improved financial outcomes.

By applying the Resource-Based View (RBV) and Technology Acceptance Model (TAM), this study demonstrates that digital financial capabilities function as strategic resources, enhancing decision-making, operational efficiency, and overall SME competitiveness. This underscores that improving digital financial literacy is not merely a technical enhancement but a strategic lever for achieving sustainable business growth.

6.1. Policy Recommendations

Policymakers, financial institutions, and development agencies should implement targeted interventions to foster both digital financial knowledge and usage. Such initiatives can help SME operators make informed decisions, optimize operations, and contribute to broader economic development in Sri Lanka.

6.2. Limitations of the Study

The study is limited by a small sample size, convenience sampling, self-reported data, and focus on a single district (Kurunegala), which restricts generalizability to the wider SME population in Sri Lanka.

6.3. Future Research Directions

- Conduct studies across multiple districts to assess the generalizability of findings.
- Investigate additional digital capabilities, such as e-commerce literacy, digital marketing, or data analytics, and their influence on SME performance.
- Undertake longitudinal research to examine how improvements in digital financial literacy and usage affect SME growth and sustainability over time.

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