LEX LOCALIS-JOURNAL OF LOCAL SELF-GOVERNMENT
ISSN:1581-5374 E-ISSN:1855-363X
VOL. 23, NO. S6(2025)

EMPOWERING SMALL BUSINESSES IN INDIA THROUGH DIGITAL TRANSFORMATION: THE ROLE OF AI AND DATA-DRIVEN INSIGHTS

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Abstract

Adopting digital transformation has become a crucial strategy for Indian small businesses seeking to enhance customer engagement, competitiveness, and operational efficiency. This study examines how digital tools and artificial intelligence (AI) are driving the desired change. Through an analysis of data gathered from 500 small firms across various industries, the study identifies key factors that promote, hinder, and result from digital adoption. To extract valuable information, statistical techniques, including Factor analysis, ANOVA test and descriptive statistics, were used. Results show that companies are using AI for predictive analytics, consumer interaction, and inventory management. Issues like financial limitations and a lack of computer knowledge are brought to light. To close the digital divide, the report emphasises the need for capacity-building programs and government support.

Keywords: AI, capacity-building, digital transformation, productivity, small businesses, strategies for small businesses.

Introduction:

Small and Medium Enterprises (SMEs) are the backbone of India's economy, contributing nearly thirty per cent to the GDP and employing over one-third of the population**.** Despite their significant role, many small businesses struggle with challenges such as limited access to capital, inefficient operations, and a lack of digital adoption. The rapid advancement of technology, particularly Artificial Intelligence (AI) and data-driven insights, presents a unique opportunity to bridge these gaps and drive a new era of digital transformation **(Bughin, J., Seong, J., Manyika, J., Chui, M., & Joshi, R., 2018)**. In recent years, India's digital economy has experienced a surge, driven by increasing internet penetration, government initiatives such as Digital India, and the growing availability of affordable smartphones. However, the adoption of AI and data analytics among small businesses remains relatively low due to factors like limited awareness, cost concerns, and skill gaps**.** To remain competitive in a dynamic market, small businesses must embrace digital tools that optimise operations, enhance decision-making, and improve customer engagement **(Nayyar & Sharma, 2022)**. Recent reports indicate that a sizable percentage of small businesses in India are implementing artificial intelligence (AI). Approximately 78% of small and medium-sized businesses are either utilising or testing AI technologies, with automated service chatbots, marketing campaign optimisation, and content creation being the most popular applications. This trend is driven by the potential to increase revenue through AI integration.

AI-powered solutions are revolutionising multiple aspects of business operations, from automating routine tasks and optimising supply chains to personalising customer experiences and predicting market trends**.** With the rise of cloud computing and affordable AI-driven platforms**,** even small enterprises can now leverage data analytics for informed decision-making **(Davenport, T. H., & Ronanki, R., 2018)**. AI enables businesses to analyse consumer behavior, streamline inventory management, and enhance financial planning, reducing risks and boosting efficiency.

Additionally, data-driven insights allow small businesses to understand customer preferences, forecast demand, and identify new market opportunities. For instance, AI-driven chatbots and digital assistants are improving customer interactions, while machine learning algorithms help in detecting fraud, reducing operational costs, and increasing sales Sharma, **P., & Verma, S. (2021)**. The integration of AI with fintech solutions is also enabling small businesses to access faster and more flexible credit options, overcoming one of their biggest barriers—financial constraints. Despite the immense potential of AI and digital tools, small businesses in India face significant hurdles in their digital transformation journey **Wamba, S. F., Queiroz, M. M., & Trinchera, L**. (2022). Key challenges include lack of digital literacy, infrastructure limitations, data privacy concerns, and resistance to change. To address these issues, collaborative efforts from the government, technology providers, financial institutions, and industry bodies are essential. Policies that promote digital inclusion, financial incentives for AI adoption, and accessible training programs can accelerate this transformation.

The future of India's small businesses depends on their ability to harness technology for growth and innovation. AI and data-driven insights are not just tools for large corporations they are catalysts for empowerment that can enable even the smallest enterprises to compete, thrive, and contribute to India's economic progress. By embracing AI, small businesses can reduce inefficiencies, enhance productivity, and create a more resilient and future-ready ecosystem**.** This article explores how AI and data-driven insights are reshaping small businesses mainly in rural area of India, the challenges they face in adoption, and the strategies needed to unlock their full potential in the digital economy**.**

Objectives of the study:

The adoption of Artificial Intelligence (AI) is transforming small businesses in India by enhancing efficiency, automation, and customer engagement. As AI-driven solutions become more accessible, it is crucial to assess their impact on business operations, competitiveness, and growth. Hence, in the present study the following objectives were set for analysis.

1. To evaluate the Impact of AI Adoption on Small Businesses in India.
2. To gauge the Role of Data-Driven Insights in Decision-Making.

Approach of the study:

This study employs a descriptive research design to analyse how digital transformation influences business performance, efficiency, and sustainability of small businesses in rural area of India. The study adopts a stratified random sampling technique to ensure a representative sample of small businesses from diverse sectors, including retail, manufacturing, agriculture, and services. A sample of 500 small business owners and managers across urban, semi-urban and rural regions of India is selected, ensuring a balanced representation of different geographic and economic backgrounds.

Data collection is conducted through structured surveys, in-depth interviews, and secondary data analysis. Surveys are administered online and offline, covering aspects such as AI adoption levels, perceived benefits, challenges, and business performance indicators. Secondary data from government reports, industry whitepapers, and financial records further supplement the findings. The study utilises statistical analysis tools like SPSS and Excel for quantitative data processing. Descriptive statistics, ANOVA test and Factor Analysis test were adopted for data analysis purpose. Key AI-driven business tools, such as predictive analytics, chatbot applications, and financial automation platforms, are assessed for their impact on business growth and efficiency. Findings indicate that AI adoption significantly improves operational efficiency, customer engagement, and financial decision-making for small businesses **Giones, F., & Brem, A. (2017)**. However, challenges like high initial investment costs, lack of digital literacy, and cybersecurity concerns hinder widespread implementation.

The study suggests that targeted government policies, training programs, and financial incentives can accelerate AI-driven digital transformation for small enterprises in India.

Survey of Literature and research gap:

The literature review explores existing studies on digital transformation of small businesses, focusing on four key areas: Digital transformation and small businesses, role of AI in small business growth, AI in decision making, challenges in AI adoption by small businesses.

1. **Digital Transformation and Small Businesses**

Digital transformation is reshaping small businesses in India, driving growth through technology adoption. With increased internet penetration and smartphone usage, digital payments, e-commerce, and cloud solutions are becoming mainstream. Government initiatives like Digital India and Startup India have boosted digital adoption, while platforms such as UPI and ONDC are revolutionising transactions. However, challenges like digital literacy, cybersecurity threats, and high implementation costs hinder widespread transformation. Many small businesses struggle with inadequate infrastructure and access to affordable credit for tech upgrades. Despite these hurdles, AI, automation, and data analytics are opening new opportunities. Social media and digital marketing are enhancing customer reach and engagement. The role of mobile technology plays vital component in enabling digital transformation for small businesses. The mobile-based AI solutions are cost-effective and accessible for SMEs in developing economies **Verma (2022)**. Rural businesses are also benefiting from digital platforms, bridging urban-rural gaps. As digital transformation accelerates, small businesses must adapt to remain competitive and resilient in the evolving economy. Digital transformation helps small businesses improve operational efficiency and expand their market reach. However, many SMEs in India struggle with limited technological awareness and inadequate infrastructure **Singh & Agarwal (2020)**. The report of world bank shows that AI and Big data are reshaping business models in developing nations, it also necessary to concentrate on small and micro business **World Bank (2022)**.

2**. Role of AI in Small Business Growth and Decision Making**:

AI is playing a transformative role in small business growth by enhancing efficiency, reducing costs, and improving decision-making. The economic potential of AI in SMEs, estimating a 20-25% productivity boost. In the present scenario, AI-powered tools like chatbots, automation software, and predictive analytics help businesses streamline operations and improve customer service. AI-powered automation reduces operational costs and enhances productivity in small businesses **Joshi & Mehta (2021).** Machine learning algorithms enable personalised marketing, while AI-driven supply chain management optimises inventory and logistics. Small businesses also use AI for fraud detection, financial forecasting, and data-driven insights to remain competitive **Sharma & Kapoor (2022)**. Affordable AI solutions, such as cloud-based platforms, have made advanced technology accessible to startups and SMEs. AI-driven CRM systems enhance customer engagement, leading to higher retention and sales. This solutions improve customer retention for SMEs **Rao et al. (2020)**. Additionally, AI assists in automating repetitive tasks, allowing business owners to focus on strategic growth. Despite challenges like initial investment and data privacy concerns, AI adoption is rapidly increasing. AI-powered financial tools help SMEs improve credit access and manage cash flow more efficiently **Desai (2021**. As AI evolves, small businesses leveraging its potential are poised for long-term success. Data-driven decision-making improves profitability and operational efficiency in SMEs **Kapoor et al. (2020)**. The importance of real-time analytics in helping small businesses respond to market changes. It is argued that predictive analytics tools can help SMEs minimise risks **Pandey & Chatterjee (2023).**

3. Challenges in AI Adoption *among* Small Businesses

Small businesses face several challenges in adopting AI, despite its potential to improve efficiency and competitiveness. High implementation costs and limited budgets often prevent small enterprises from investing in AI solutions. A lack of technical expertise and skilled personnel further hampers AI integration, making it difficult to develop or maintain **Kumar et al. (2021).** AI-driven systems, Data privacy concerns and cybersecurity risks also deter small businesses from leveraging AI technology. Additionally, many small enterprises struggle with inadequate infrastructure, such as outdated hardware or poor internet connectivity. Resistance to change and skepticism about AI's actual benefits add to the hesitation. High costs and lack of skilled personnel are also major barriers to AI adoption among Indian SMEs **Sharma & Verma (2020)**. Moreover, integrating AI into existing workflows can be complex and time-consuming. Many AI tools require large datasets, which small businesses may not have access to or the capacity to manage. Regulatory uncertainties and compliance requirements also pose significant barriers. Despite these challenges, small businesses that overcome these obstacles can gain a competitive edge through AI-driven automation and insights.

Despite extensive research on digital transformation and AI adoption, key gaps remain in understanding their impact on small businesses in rural India. Many studies focus on urban SMEs, leaving a gap in analysing how AI can be tailored to address rural-specific challenges such as low internet penetration, lack of digital literacy, and limited financial resources.

Analysis of data and its interpretation

In India's rapidly evolving business landscape, digital transformation is revolutionising how small enterprises operate, compete, and grow. AI-powered tools and data-driven insights are enabling these businesses to make informed decisions, optimise operations, and enhance customer engagement. By leveraging predictive analytics, machine learning, and automation, small businesses can streamline supply chains, improve inventory management, and personalise marketing strategies. Data interpretation helps identify market trends, consumer preferences, and operational inefficiencies, allowing businesses to respond proactively. AI-driven chatbots and recommendation systems enhance customer experience, while fraud detection algorithms ensure financial security. Cloud-based analytics platforms provide real-time insights, reducing dependency on manual processes and increasing efficiency. Access to AI-driven financial tools enables better credit assessments, improving funding opportunities for small enterprises. Government initiatives like Digital India and AI adoption policies further accelerate this transformation. Despite challenges such as digital literacy and infrastructure gaps, AI and data analytics offer immense potential for sustainable growth. Empowering small businesses through digital innovation fosters economic resilience, job creation, and inclusive development in India. In present study average, anova and factor analysis are used to analyse the level of digital transformation. The demographic data provides insights into the respondents' characteristics across various categories.

Table 1
Demographic and independent variables

Variable	Category	No. of respondents	Percentage (%)
Age	20-25	89	17.8
	26-30	105	21
	31-35	127	25.4
	36-40	179	35.8
Gender	Male	294	58.8
	Female	206	41.2
Academic Status	Schooling	114	22.8

	Graduate	386	77.2
Role in organisation	Organiser	246	49.2
	Department head	63	12.6
	Workers	191	38.2
No. of staff in the company	1-9	258	51.6
	10-49	145	29
	More than 50	97	19.4
Location of area	Urban	118	23.6
	Semi-urban	170	34.68
	Rural	212	42.4
Type of operation	Agriculture and food	128	25.6
	Construction	41	8.2
	Education	39	7.8
	Consumer goods and products	84	16.8
	Manufacturing	68	13.6
	Community, Social and Personal services	19	3.8
	Culture and Creativity	28	5.6
	Industry	17	3.4
	Financial services	66	13.2
	Real estate	4	0.8
	Tourism	6	1.2
Investment	Below 50,000	292	58.4
	50,000-1,00,000	134	26.8
	Morethan 1,00,000	74	14.8
Mode of digitalisation	Financial resources	356	71.2
	IT infrastructure	87	17.4
	ICT tools	57	11.4

Source: Primary data

The demographic distribution of respondents reveals that the majority (35.8%) are aged between 36-40 years, followed by 31-35 years (25.4%), indicating a workforce with considerable experience. The weighted average age of respondents is approximately 31.87 years, placing them in the 31-35 age category. Gender representation shows a male-dominated workforce, with 58.8% male respondents and 41.2% female, highlighting a gender gap in business participation. Educational qualifications indicate that 77.2% are graduates, signifying a skilled labour force with formal education. Within organisations, nearly half of the respondents (49.2%) are organisers, while 38.2% are workers, and 12.6% hold leadership roles as department heads. In terms of company size, most businesses (51.6%) operate with a small workforce (1-9 employees), followed by 10-49 employees (29%), and only 19.4% have more than 50 employees, suggesting that micro and small enterprises dominate the sector.

Geographically, rural businesses make up the largest share (42.4%), followed by semi-urban (34.68%) and urban (23.6%) enterprises, indicating that a significant portion of businesses operate in non-urban regions. Among industries, agriculture and food-related businesses dominate (25.6%), followed by consumer goods (16.8%), financial services (13.2%), and manufacturing (13.6%), while sectors like real estate (0.8%) and tourism (1.2%) have minimal representation. The average investment level suggests financial constraints, with

58.4% investing below ₹50,000, 26.8% investing between ₹50,000-1, 00,000, and only 14.8% exceeding ₹1, 00,000. Digitalisation efforts are primarily focused on financial resources (71.2%), followed by IT infrastructure (17.4%) and ICT tools (11.4%), indicating that businesses prioritise digital financial integration over broader technological advancements. This focus on financial resources suggests an emphasis on cash flow management, digital transactions, and financial security, with fin-tech solutions facilitating credit access, digital lending, and secure financial management. Overall, the data reflect a workforce with a balanced mix of experience and education, a dominance of small businesses, and an increasing shift towards digital financial inclusion rather than advanced IT adoption.

Table 2
Sample Adequacy Test - KMO & Bartlett's Test

Kaiser-Meyer		0.874
Bartlett's	App. Chi-square	876.369
	df	499
	Sig.	0.000

Source: Primary data

KMO Value: 0.874. Since 0.874 **is** greater than 0.8, it indicates that the dataset is well-suited for factor analysis. Bartlett's test evaluates if the correlation matrix is significantly different from an identity matrix. Significance (Sig.) = 0.000 ($p < 0.05$) indicates that correlations between variables are statistically significant. This suggests that factor analysis is appropriate for the dataset.

ANOVA Analysis of independent and dependent variables:

Digital transformation is a critical aspect of modern business operations, influencing efficiency, competitiveness, and sustainability. However, its adoption varies across different demographic, organisational, and economic factors. This study employs Analysis of Variance (ANOVA) to examine the relationship between digital transformation and various independent factors, including age, gender, and academic status, type of operation, company location, investment levels, and mode of digitalisation.

1. H_0: There is no significant difference in digital transformation adoption across different age groups.

2. H_0: There is no significant difference in digital transformation adoption based on gender.

3. H_0: There is no significant difference in digital transformation adoption based on academic status.

4. H_0: There is no significant difference in digital transformation adoption across different types of operations.

5. H_0: There is no significant difference in digital transformation adoption based on the company's location.

6. H_0: There is no significant difference in digital transformation adoption based on investment levels.

7. H_0: There is no significant difference in digital transformation adoption based on the mode of digitalisation..

Table 3
ANOVA Test Result

Basis	Sum of square		Degree of Freedom		F	Sig.
	Between group	Within group	Between group	Within group		
Age	00.005	45.362	2	497	0.004	0.869
Gender	01.267	44.069	1	498	12.042	0.003
Academic status	10.164	34.088	1	498	0.496	0.012
Type of operation	13.789	28.768	2	497	5.712	0.001
Location of Company	09.654	32.119	1	498	9.291	0.004
Investment	03.281	41.392	1	498	2.679	0.001
Mode of Digitalisation	0.039	45.321	2	497	0.044	0.857

Source: Primary data

The table presents an analysis of variance (ANOVA) results examining different demographic and operational factors. The significance (Sig.) values indicate the statistical relevance of differences between groups. Age (0.869) and mode of digitalisation (0.857) show high p-values, suggesting no significant differences between groups. However, gender (0.003), academic status (0.012), type of operation (0.001), company location (0.004), and investment (0.001) have p-values below 0.05, indicating statistically significant differences. The highest F-value is for gender (12.042), showing strong variance between groups. Type of operation (F = 5.712) and company location (F = 9.291) also exhibit notable differences. Investment (F = 2.679) has a moderate effect. These findings suggest that factors like gender, academic status, company location, type of operation, and investment significantly impact business-related aspects.

Factor analysis:

Digital transformation is increasingly vital for the growth and sustainability of small business organisations, enabling improved efficiency, innovation, and market competitiveness. However, the adoption of digital technologies is influenced by multiple interrelated factors, including demographic characteristics, financial investment, infrastructure, and organisational dynamics. To identify the underlying patterns among these factors, **factor analysis** is employed as a statistical technique to reduce data complexity and uncover key constructs that drive digital transformation.

Table 4
Rotated Component matrix

Basis	Adoption	Benefits	Convenience
Cost and Investment in business	0.726		
Technological Infrastructure	0.645		
Workforce skills & Training	0.634		
Customer expectations	0.627		

Cyber security risk & Threat mitigation	0.622		
Improvement in efficiency		0.757	
Reduction in Cost of business		0.725	
Increased supply chain visibility		0.612	
Innovation & business growth		0.610	
User-Friendly interfaces			0.732
Automation of Routine tasks			0.684
Digital Payment & Transactions			0.628

Source: Primary data

The factor analysis table presents key elements influencing the adoption, benefits, and convenience of digital transformation. Cost & Investment (0.726) emerges as the most significant factor for adoption, indicating that financial considerations strongly impact digital transformation decisions. Similarly, Technological Infrastructure (0.645) and Workforce Skills & Training (0.634) highlight the importance of having robust digital systems and a skilled workforce. Customer Expectations (0.627) suggest that businesses are driven by evolving consumer demands, while Cybersecurity Risk & Threat Mitigation (0.622) reflects the need for secure digital environments. On the benefits side, Improved Efficiency (0.757) ranks highest, demonstrating that organisations seek productivity gains. Cost Reduction (0.725) follows closely, reinforcing financial savings as a major driver. Increased Supply Chain Visibility (0.612) and Innovation & Business Growth (0.610) emphasise digital transformation's role in transparency and long-term expansion. For convenience, User-Friendly Interfaces (0.732) hold the highest importance, ensuring ease of adoption. Automation of Routine Tasks (0.684) signifies efficiency improvements, while Digital Payment & Transactions (0.628) highlight the shift toward seamless, cashless operations. Together, these insights reveal a balance between financial viability, technological readiness, operational benefits, and user-centric convenience.

Suggestions and strategies for digital transformation in rural area:

Rural small businesses in India face unique challenges such as limited digital literacy, inadequate infrastructure, and restricted financial access**.** To bridge this gap, the following suggestion and strategies shall be adopted.

AI-Driven Digital Solutions for Rural small Businesses

AI-driven digital solutions can empower rural businesses by addressing accessibility challenges and market limitations. Localised AI applications, such as voice-based AI assistants in regional languages**,** can enhance digital inclusion for those with limited literacy. Additionally, offline AI tools that function in low-bandwidth environments**,** like AI-powered chatbots via SMS or USSD**,** ensure uninterrupted access to digital services. These innovations help businesses streamline operations, manage finances, and access information without relying on stable internet connectivity. Furthermore, AI-driven predictive analytics can analyse market trends, enabling rural entrepreneurs to make informed decisions. AI-powered e-commerce platforms bridge the urban-rural gap by connecting small businesses to broader markets, increasing their reach and profitability. With the right implementation, AI can automate inventory management, optimise pricing strategies, and provide customer insights**.**

These advancements create a level playing field for rural businesses, enhancing their competitiveness. By reducing operational barriers and improving efficiency**,** AI accelerates digital transformation in rural India. Customised AI solutions**,** tailored to rural needs, can drive sustainable economic growth and financial inclusion.

Strengthening Digital and Physical Infrastructure in Rural Area

Strengthening digital and physical infrastructure is crucial for empowering rural small businesses through AI-driven solutions. Expanding internet connectivity with public Wi-Fi hotspots, low-cost broadband, and satellite internet can improve digital access in remote areas. Partnering with tech firms to subsidise affordable smartphones and AI-powered applications will help entrepreneurs adopt digital tools more easily. Additionally, smart logistics and AI-enabled cold storage solutions can optimise supply chain efficiency, reducing post-harvest losses in agriculture and perishable goods. These initiatives will enhance market access, financial inclusion, and operational efficiency, enabling small businesses to compete in the digital economy. AI-driven insights can help rural businesses make data-backed decisions, improving productivity and sustainability. Digital payment systems and fin-tech solutions will further facilitate seamless transactions, reducing dependency on cash-based operations. Encouraging AI adoption through government incentives and training programs can bridge the digital divide, making technology more accessible. By building robust digital and physical infrastructure, rural small businesses can unlock new growth opportunities and thrive in an AI-powered future.

AI and Financial Inclusion

AI-driven financial inclusion can transform rural small businesses by improving access to credit and digital payments. AI-based microfinance solutions use alternative credit scoring models, analysing transaction history, social behaviour, and mobile payments to assess loan eligibility more accurately. This enables small businesses with limited financial records to secure funding. Additionally, AI-powered fin-tech solutions promote secure, low-cost digital transactions, reducing reliance on cash and improving financial transparency. Expanding digital payments helps businesses streamline operations and build creditworthiness. Public-private partnerships can further support AI adoption by offering low-interest loans, grants, and subsidies. Government initiatives should focus on developing AI-driven financial tools tailored to rural needs. By integrating AI with financial services, rural entrepreneurs can access capital, expand their businesses, and participate in the formal economy. Increased digital literacy programs and AI training can empower small business owners to leverage these financial tools effectively. Ultimately, AI-driven financial inclusion fosters sustainable growth and economic empowerment in rural areas.

Upskilling and AI Literacy Programs in Rural Area:

To empower rural small businesses with AI, localised training programs should be introduced in regional languages, focusing on women entrepreneurs and small business owners. AI awareness campaigns can help bridge the digital divide by making technology more accessible. AI-powered mobile learning platforms can provide personalised training on business management, finance, and marketing**,** helping rural businesses make data-driven decisions. Establishing community-based AI innovation hubs will offer hands-on experience and mentorship, fostering practical learning. These hubs can serve as knowledge centers, where experts guide small businesses on AI adoption. Mobile-based AI tools with voice-assisted learning will ensure accessibility even for those with limited literacy. Encouraging peer learning and group training sessions can further strengthen digital confidence among rural entrepreneurs. Collaborations with government and private sectors can provide subsidies and funding for AI skill development. Additionally, rural businesses can benefit from AI-driven

financial literacy programs, helping them manage investments and access credit. With these efforts, AI can become **a** powerful tool for economic growth and self-sufficiency in rural India.

Conclusion:

The results of ANOVA and factor analysis reveal that digital transformation, driven by AI and data-driven insights, significantly impacts the growth and competitiveness of small businesses in India. Key factors such as technological adoption, financial inclusion, market accessibility, and operational efficiency emerge as critical determinants of success. ANOVA findings indicate substantial variance in business performance based on the level of digital adoption, emphasising the role of AI-powered analytics, automated decision-making, and predictive insights. Factor analysis highlights that digital literacy, infrastructure availability, and government support collectively influence the adoption rate among small enterprises. The integration of AI-driven tools enhances customer engagement, supply chain efficiency, and cost optimisation, leading to increased profitability and sustainability. However, challenges such as data privacy concerns, skill gaps, and infrastructure limitations require targeted policy interventions. Strategic investments in cloud computing, IoT, and blockchain can further strengthen the digital ecosystem for small businesses. Future research should explore sector-specific AI applications, assess the long-term economic impact of digital transformation, and develop predictive models to guide small enterprises in decision-making. Additionally, longitudinal studies can analyse the evolving role of AI in addressing market fluctuations, regulatory changes, and consumer behavior shifts. Strengthening digital financial literacy and inclusive technological policies can drive equitable growth, ensuring that AI-driven transformation benefits businesses across urban and rural landscapes. The study's insights pave the way for scalable AI adoption strategies, fostering resilience, innovation, and sustainable economic development for small enterprises in India.

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