

## Factors Affecting on Business Failure of 3PL Companies in Sri Lanka

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**Abstract** - Sri Lanka, Small & Medium Enterprises (SMEs) contribution to GDP and employment generation is over 70 percent. As per the previous studies done by Lussier, Bandara and Marom (2016), 45 percent of the businesses (Small & Medium Enterprises) fail in Sri Lanka. According to literature, failed companies are defined for the research as, failed or potential to fail companies & SBU (Strategic Business Units), where a company is in liquidation, loan default, credit risk, financial distress, payment issues to suppliers or lenders and having a nonperforming business unit. The main objective of this study is to explore the factors affecting business failures of 3PL (Third Party Logistics) companies in Sri Lanka. As Literature suggests, inadequate resources, poor financial management, inefficient strategic management, Poor administration & human resources management, poor adaptability to the external environment, poor customer-supplier relationships are the factors affecting on business failure situations, which are considered as independent variables for the study. The dependent variable is the business failure in 3PL companies of Sri Lanka. A Sample frame of 135 fail or nonperforming companies or Strategic Businesses Units (SBU) in Sri Lanka was used for the study. Primary data was collected through structured questionnaires using seven-point Likert scale, from the entrepreneurs and managers of fail and non-performing companies of Sri Lanka. The quantitative data analysis was done using SPSS (23). Univariate, Bivariate and Multivariate analysis used for data analysis and due to dependent variable date are categorical, ordinal data, ordinal logistic regression is used to explore the impact of relationship between the dependent variable and independent variables. The study concludes that independent variables, inadequate resources, poor financial management, inefficient strategic management, poor administration & Human Resources and poor customer-supplier relationships are the significant factors affecting business failure in 3PL companies.

**Key Words:** Business Failures, 3PL, customer-supplier relationships

### I. INTRODUCTION

Globally the failure rates of businesses are increasing. It negatively affects the economy since entrepreneurs contribute to economic growth. As a result, the need arise for successful entrepreneurs than failure entrepreneurs in order to enhance the economic growth and to reduce wastage of valuable resources. Entrepreneurs play a major role in economic development (Tomaa, Grigorea and Marinescu, 2013). As shown in Table 1 statistics shows that contribution by the SME's to Sri Lankan economy is more than that of Malaysia, Singapore and Japan (Bandara, 2016).

Source: Nasirembe (2013) & Ministry of Finance (2012) cited in Banadara (2016) pg.1

(<http://www.dailymirror.lk/101755/what-causes-smes-to-fail-in-sri-lanka> (p:1)

#### A. Problem Statement

Sri Lanka emerging as a key sourcing base in South Asia for international buyers resulting in increase in demand for 3PL services, including warehousing and transportation as well as integrated supply chain solutions (Hong Kong Research Trade Development Council, 2015). Further Sri Lanka possess Location advantage by lying in the Silk route /East-West trade route which is needed to develop in to key logistics hub in South Asia. According to Hong Kong Research Trade Development Council (2015), World Shipping Council statistics shows that the Colombo port as the Sri Lanka's major container port on the west coast and further was the busiest port in South Asia in 2013. It was handling 4.31 million Twenty Equivalent units (TEUs). Hence this has put it ahead of India's largest container port

Table 1 – Economic Contribution by SMEs

Country	Establishments (%)	Employment (%)	GDP (%)
Malayasia (2010)	99.2	56	32
Japan (2010)	99.7	69.5	55.3
Singapore (2010)	90	56	42
Sri Lanka (2010)	80 - 90	>70	>70

Jawaharlal Nehru, which was handling only 4.12 million Twenty Equivalent units TEUs in 2013. Thus in various literature it has been discussed that Sri Lanka having all the facilities such as high demand, infrastructure, access to information technology, man power, access to capital in order to continue as successful 3PL business companies and have greater demand to move towards 4PL business companies. Today the 3PL market has moved to 7PL (Yap, 2008). Sri Lanka is one of the countries in which logistics and supply chain management knowledge is available with citizens and with good standard universities and institutes. Nevertheless many of the Sri Lankan 3PL business companies or 3PL strategic business units (SBU) are either bankrupt or moved to other businesses or fail to service as successful 3PL companies and have not moved to the next stage to perform as 3PL or 4PL to 7PL companies with the world trend. This is evident by not having real 4PL companies in Sri Lanka. Further, according to Lussier, Bandara and Marom (2016) business failure rate in Sri Lanka is 45 percent. Moreover, according to Shabir *et al* in 2016 some 3PL businesses succeed while others end up in bankruptcy. However many questions are arising why this bankruptcy take place?

**B. Research Questions**

Based on the problem statement the research questions are developed for the study as below.

- i. What are the Challenges faced by 3PL companies?
- ii. What are the factors affecting business failure of 3PL companies?
- iii. What is the relationship between the factors affecting business failure on the 3PL companies?

**C. Research Objectives**

With reference to the research questions, the research objectives set for the study as below.

- i. To determine the Challenges faced by 3PL companies?
- ii. To assess the factors affecting business failure of 3PL companies?
- iii. To identify the relationship between the factors affecting business failure on the 3PL companies?

**D. Review of Literature**

Organizations do business in increasingly competitive world and companies are in a VUCA world (Volatile, Uncertain, Complex & Ambiguous). The organizations need to face unexpected risks, facing business failures. The business failures can have many repercussions on the organization as well as on people. According to Bill, Sonny & Susan (1994), when consider about the organizations, financial shortfalls will threaten their very

survival. And on the other hand when consider people, these crises will damage the quality of life for different groups of people associated with the organization, such as big emotional and social costs are incurred as the organization becomes a less rewarding place to work or to do business. More over, organizational restructurings, redundancies, customer delivery breakdowns, lay-offs and failures to pay creditors can occur and will worsen traditional standards of working and living for stakeholders. Hence organizations may benefit from the research as a whistle blower. Moreover it is important for the policy makers of the government to realize the successfulness of the companies since the 3PL companies has a wide contribution to the society as well as it's significant share to the local employment market, resource distribution, supply chain to the country. 3PL companies are widely used by majority of the private sector businesses as well. Day today needs & wants of people, and the things in their vicinity are either imported by one of these 3PL companies or manufactured and sold in the local market or these 3PL companies export excess production. Further the research information is useful not only for small investors but for major investors such as Shangrilla Hotels, Apple computers, to decide the amount of resource allocation for each business based on the local characteristics in order to avoid failures. More over this research findings can be used to remove the obstacles in the journey of marching towards the 7PL.

**II. METHODOLOGY AND EXPERIMENTAL DESIGN**

**A. Conceptual Framework**

Based on the hypothetical behavioral pattern, the proposed conceptual framework is depicted in Figure 1 below.

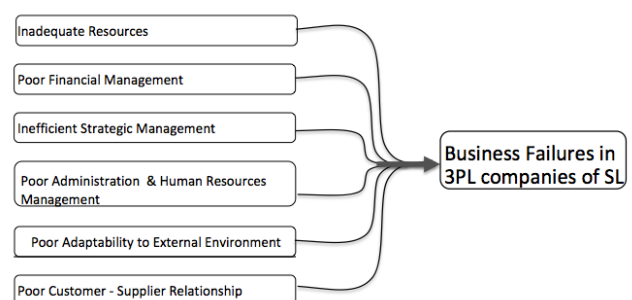


Figure 1: Factors affecting 3PL companies in Sri Lanka & their effect

Source: Developed by the Author (2019)

According to Figure 1, inadequate resources (Hyder and Lussier, 2016; Baidoun *et al*, 2017; Kraybill, Nolt and Wesner, 2011) poor financial management (Baidoun *et al*, 2017; Pardo, C. & Alfonso, W. 2017), inefficient strategic management (Baidoun *et al*, 2017; Lussier, Bandara and Marom 2016; Sridevi and Kumar, 2015;

Hyder and Lussier, 2016; Cui *et al*, 2018), Poor administration & human resources management (Pardo and Alfonso, 2017; Boostrom *et al*, 2011), poor adaptability to external environment (Hyder and Lussier, 2016; Pardo and Alfonso, 2017; Cruz *et al*, 2018.) and poor customer- supplier relationships (Teng, Bhatle and Anwer, 2011; Malkanthie and Jayamanna, 2016) are the independent variables for the dependent variable, “business failure in 3PL companies of Sri Lanka”.

**B. Formulation of Empirical Model**

The formulation of the empirical model of the research was developed based on the conceptual framework of the study as shown below.

$$Y_i = f(\beta_{xi}, \beta_{xi2}, \beta_{xi3}, \beta_{xi4}, \beta_{xi5}, \beta_{xi6}) \text{ Err}$$

Where;

- Y = Vectors of 3PL Business failure
- X1 = Vectors of Inadequate resources
- X2 = Vectors of poor financial management
- X3 = Vectors of poor supply chain management
- X4 = Vectors of poor Administration & HR decisions
- X5= Vectors of poor adaptability to external environment
- X6 = Vectors of poor customer- supplier relationships
- i = In an organization
- Err = Error term

For this study the population is unknown and sample frame is based on a database collected from a reliable source, which consist of 135 fail or potential to fail 3PL companies or SBUs of Sri Lanka. The research is conducted based on quantitative method. The researcher use simple random sampling method to collect the quantitative data in order to perform quantitative analysis. The sampling element used is the entrepreneurs and managers. The data is collected using a questionnaire method.

**C. Sample Profile**

A sample of 61 fail companies, potential to fail companies or Strategic Businesses Units (SBU) in Sri Lanka was used for the study.

**D. Data Collection**

In quantitative method the primary data is collected using survey method, using the structured questionnaire. The structured questionnaire is prepared with 78 questions based on the conceptual framework and the Operational Table. The structured questionnaire is mainly based on 7-point staple scale questions. Researcher pre-tested the questionnaire to ensure consistency and relevance of questions with managers and industry experts in the logistics industry and with the supervisor. The questionnaires were distributed to respondents using Google forms in order to fill through electronic media and distributed hard copies to fill

manually depending on the respondent’s convenience in order to get the responses. The secondary data was collected for the literature review from published records such as published researches, published articles and papers, textbooks and journals.

**E. Data Analysis**

The collected data will be checked for reliability of scale to ensure the goodness of data. ‘Statistical Package for Social Sciences’ (SPSS) will be used as a statistical tool to analyze the collected data. Mainly dependent variable data are categorical ordinary data and thus data analysis will be done using ordinal logistic regression model to explore relationships between the dependent variable and the six independent variables. Multi-variate analysis is performed using Pseudo R<sup>2</sup>, Model fit, reliability testing, sample adequacy, coefficient analysis and Logistic Regression. Pseudo R<sup>2</sup> is used to check the goodness of fit, where it measures the contribution of independent variable for a change in dependent variable by 1 unit. Use Model fit to identify whether the independent variables can observe the changes of dependent variable.

**III. RESULTS**

**A. Estimation of Sample Adequacy**

Sample size adequacy is checked using Kaiser-Meyer-Olkin the measure of sampling Adequacy test (KMO). The standard value for KMO is a value between 0 and 1. And KMO value being closer to a value of “one” greater the adequacy. As shown in Table 2, the KMO is 0.805 at 0.000 significance level and degree of freedom of 21. Thus the sample is well adequate.

Table 2: Sample size adequacy –KMO & Bartlett’s Test

KMO and Bartlett's Test	
Kaiser-Meyer-Olkin Measure of Sampling Adequacy.	.805
Bartlett's Test of Sphericity	Approx. Chi-Square
	Df
	Sig.
	21
	.000

Source: Survey data (2019)

**B. Assessment of Internal Consistency**

Reliability and Internal consistency of the collected scale data is tested using Cronbach’s Coefficient Alpha, which gives an indication whether respondents have understood the survey questions in the same way and how the items are interrelated. Further it indicated to which extent the results would be the same with repeated tests. Cronbach’s Alpha shows how closely a set of items and it’s subset of items are inter related in a group and it range from 0 to 1 and higher the value it

indicates the greater the reliability and internal consistency. In theoretical studies, even a figure of 0.60 or 0.50 acceptable (Nunnally, 1967).

Table 3: Reliability Statistics for Survey data – Cronbach Alpha

Reliability Statistics	
Cronbach's Alpha	N of Items
.941	59

Source: Survey data (2019)

As shown in Table 3, the total survey has resulted a Cronbach Alpha of 0.941, which is acceptable and it indicates that all respondents have understood the survey questions in a similar way and is highly reliable.

The variables were tested separately too in order to check the reliability of the input & output data. When tested the variables separately researcher found, 0.706 for resource profile, 0.839 for financial management profile, 0.847 for strategic management profile, 0.746 for administration & HR profile, 0.759 for the environmental profile, 0.868 for customer- supplier relationships profile and 0.684 for the dependent variable.

C. The Estimation of Empirical Model

The survey data is analyzed using the ordinal regression analysis. The estimation of empirical model was done using Ordinal Regression Logit Model. Table 4 shows the factors surveyed under resource profile.

Table 4 Results of Ordinal Regression – Resource Profile

	Estimate	Std. Error	Wald	df	Sig.	95% Confidence Interval	
						Lower Bound	Upper Bound
Impact of skilled staff TO	-6.335	3.515	3.249	1	0.07	-13.223	0.554
Non availability of capital	-2.524	3.132	0.65	1	0.42	-8.663	3.614
Reluctant for outside professionals	-1.843	1.406	1.717	1	0.19	-4.599	0.913
Customer Shift to competitor	8.947	3.515	6.479	1	0.01	2.058	15.836
High employee TO	3.932	2.486	2.503	1	0.11	-0.939	8.804
Inadequate capacity to fulfill orders	4.175	3.192	1.711	1	0.19	-2.081	10.431
Delay in fulfilling orders	6.37	5.306	1.441	1	0.23	-4.03	16.77
Inadequate human resources	2.411	3.243	0.553	1	0.46	-3.945	8.766
Poor internet lead to delay orders	0.388	1.705	0.052	1	0.82	-2.955	3.73
Inexperience staff create dissatisfied customers	0.466	3.246	0.021	1	0.89	-5.895	6.827

Source: Survey Data (2019)

As per the Table 4 impact of skilled staff turnover, non-availability of capital and reluctant for outside professionals are inversely related to business failure in 3PL companies while customer shifting to competitor, high employee turnover, inadequate capacity to fulfill the orders, delay in fulfilling orders, inadequate human resources, delays due to poor internet facility, inexperience staff makes dissatisfied customers are the variable that are factors which influence positively to

business failure in 3PL companies. Out of all these variables customer shift to competitor is moderately positively significantly related. And this is in line with the studies done by (Malkanthe and Jayamanna, 2016) where they found the high employee turnover as a major reason for business failure.

When consider the Finance Management Profile, the ordinal regression results are shown below in Table 5.

Table 5 Results of Ordinal Regression – Financial management Profile

	Estimate	Std. Error	Wald	Df	Sig.	95% Confidence Interval	
						Lower Bound	Upper Bound
Poor Financial Controls	-2.901	6.208	0.218	1	0.64	-15.068	9.267
Suppliers not paid on time	6.112	1.931	10.014	1	0.002	2.326	9.897
Sales targets not met	6.272	7.529	0.694	1	0.405	-8.484	21.029
Ignorance of audit reports	2.434	5.621	0.188	1	0.665	-8.582	13.45
Finance managed inefficiently	0.323	2.54	0.016	1	0.899	-4.655	5.302
Poor record keeping	0.367	3.676	0.01	1	0.92	-6.837	7.571

Source: Survey Data (2019)

As shown in Table 5, financial management profile other than the poor financial control the indicators such as suppliers not paid on time, sales targets not met, ignorance of audit reports, financial managed

inefficiently, poor record keeping are directly related. Out of all these elements financial control upon supplier is significant. Below Table 6 depicts the effect of strategic management profile on the 3PL business company failure.

Table 6 Results of Ordinal Regression – Strategic Management Profile

	Estimate	Std.Error	Wald	df	Sig.	95%Confidence Interval	
						Lower Bound	Upper Bound
Doesn't have a strategic plan	-4.807	7.327	0.431	1	0.512	-19.167	9.552
Not having the optimum products range	-4.178	2.922	2.044	1	0.153	-9.905	1.549
Don't invest in advanced technology	-3.373	6.869	0.241	1	0.623	-16.836	10.091
Don't like partnerships	-0.324	1.731	0.035	1	0.852	-3.717	3.069
SBU budgets not prepared	6.444	3.233	3.972	1	0.046	0.107	12.781
Fail top management decisions	7.551	5.477	1.901	1	0.168	-3.183	18.285
Inexperienced MGM cannot save company	0.563	1.844	0.093	1	0.760	-3.051	4.177
Unskilled MGM result in BF	0.51	5.423	0.009	1	0.925	-10.119	11.138
Doesn't have business plan	0.402	8.734	0.002	1	0.963	-16.716	17.519

Source: Survey Data (2019)

As per the Table 6, not having a strategic plan or optimum product range, not willing to investing in advance technology, not willing to have partnerships are inversely related to 3PL business failure while not preparing strategic business unit (SBU) wise budgets, failure in top management decisions, inexperienced management unable to save the company, unskilled

managements result in business failure, not having a business plan are the variable factors that influence positively to business failure in 3PL companies. Out of all these, not preparing SBU wise budgets are positively & significantly related. Below Table 7 illustrates the ordinal regression Table for administration & HR Profile.

Table 7 Results of Ordinal Regression – Administration & HR Profile

	Estimate	Std. Error	Wald	df	Sig.	95%Confidence Interval	
						Lower Bound	Upper Bound
Leadership style affect performance	-4.821	2.763	3.044	1	0.081	-10.236	0.594
Size of firm affect administration	-0.097	2.135	0.002	1	0.964	-4.28	4.087
CEO don't value employees	19.393	7.948	5.954	1	0.015	3.816	34.97
Training & development not available	7.14	3.613	3.906	1	0.048	0.059	14.22
Inefficient administration lead to non performance culture	1.181	0.947	1.556	1	0.212	-0.675	3.037

Source: Survey Data (2019)

According to Table 7 other than the inversely related leadership style and size of the firm affecting the administration, the indicators such as CEO not valuing employees, non-availability of training & development and inefficient administration leading to non-performance culture is significant. This finding is in line with the literature where, Mehralizadeh and Sajady (2005) revealed, in order to retain skilled or semi-skilled employees need to orientate them and provide required

training and business mentoring. And Teng, Bhatle and Anwer (2011) too arrived at the similar findings by showing that employment, training and the retainment of high-quality staff members in the companies are the most important factors to avoid business failure for SMEs.

Below Table 8 depict the ordinal regression results of poor adaptability to external environment.

Table 8 Results of Ordinal Regression – Poor Adaptability to External Environment

	Estimate	Std. Error	Wald	df	Sig.	95%Confidence Interval	
						Lower Bound	Upper Bound
Strong competition from competitor	-5.492	4.512	1.482	1	0.224	-14.336	3.351
Company face severe competition	-4.822	4.407	1.197	1	0.274	-13.46	3.815
Company in strong industry	-3.487	4.394	0.63	1	0.427	-12.099	5.125
Government decisions result in price fluctuations	-1.475	1.933	0.582	1	0.445	-5.264	2.314
Don't have government support	8.582	4.767	3.241	1	0.072	-0.761	17.924
Don't carry marketing campaigns	6.419	5.104	1.582	1	0.209	-3.585	16.424
Need customs & government approvals	5.565	5.257	1.121	1	0.290	-4.739	15.868
Political influence to do business	2.222	2.167	1.051	1	0.305	-2.025	6.469
Government regulations affect purchasing	7.752	10.003	0.601	1	0.438	-11.853	27.357

Source: Survey Data (2019)

As shown in Table 8 while the strong competition from competitor, company face severe competition, company in strong industry and government decisions result price fluctuations are inversely related to the business failure of 3PL companies, not having government support, not caring out marketing campaigns, need customs & government approvals, political influence to do business, government regulations affect purchase prices are directly related to business failures of 3PL companies.

Below Table 9 shows the Ordinal Regression results for the poor customer-supplier relationships profile.

Table 9 Results of Ordinal Regression – Customer-Supplier Relationships

	Estimate	Std. Error	Wald	df	Sig.	95%Confidence Interval	
						Lower Bound	Upper Bound
Prohibit social media with customers	-5.809	3.457	2.823	1	0.093	-12.584	0.967
Fewer repeat orders	-0.042	4.626	0	1	0.993	-9.109	9.025
Less relationships result in less information	10.668	2.499	18.219	1	0	5.769	15.566
No incentives to employees to encourage sales	6.387	3.388	3.554	1	0.059	-0.253	13.027
Don't invest to retain customers	2.776	1.927	2.074	1	0.150	-1.002	6.554
Employees not empowered to take decisions	3.361	2.877	1.364	1	0.243	-2.278	8.999
No long term customer relationships	5.226	5.599	0.871	1	0.351	-5.749	16.201

Source: Survey Data (2019)

As Table 1.8 illustrates, other than the inversely related, prohibit to use social media with suppliers and fewer repeat orders, the less relationship resulting in less information, no incentives for employees to encourage sales, not investing to retain customers, employees not empowered for decision making and no long term customer relationships are directly related to business failure in 3 PL companies. The less relationship resulting in less information is strongly directly related to business failure of 3PL companies. This finding is in consistent with the findings of Hyder, 2016 where he found that the partnerships are important for success and to avoid failures.

#### IV. DISCUSSION AND CONCLUSION

The study focus, on the research questions such as the challenges to the 3PL companies in Sri Lanka, the factors affecting the business failure of 3PL companies and to find the relationship between the failure of 3PL companies and the identified factors affecting 3PL business failure. According to the regression analysis the most influencing independent variables on the dependent variable, business failure in 3PL companies are the 'customer-supplier relationships' with a beta value of +0.357 at 99 percent confidence level and 'financial management profile' with a beta value of +0.308 at 95 percent confidence level. However when we analyze the components of, each of the, six independent

variable using Ordinal Logistic Regression it was revealed, that the factors such as that the 'customer shift to competitor', 'suppliers not paid on time', 'SBU budgets not prepared', 'CEO don't value employees', 'training & development not available', 'less relationships result in less information' affects the business failure in 3PL companies.

According to a marketing slogan "the customer is the king". All the costs in a company recovered from the volume of the sales achieved. Thus company's losses or profitability would depend only with the action of a customer with the sales volume. Customer's attraction to the to the company depends on the 4Ps (Product, Price, Place & Promotion), customer loyalty, previous experiences of customer, customer satisfaction, discounts, value for money given. Further Balance scorecard demonstrates the value of financial & non-financial factors for a company to flourish. And according to it the customer focus is of greater importance & reviews how customer perceives the company. Hence provided the company has not supplied these financial and non-financial benefits to the customer, customer will move to competitor resulting loss of sales to the company. Thus shifting customers to competitor would be a factor affecting business failure in 3PL companies.

In current world the companies cannot work on isolation and all the companies, processes are linked together. The respective company's supply chain, is linked to customer's supply chain and to supplier's supply chain. This happened with first tire supplier, second tire suppliers. Thus when the company do not pay the suppliers on time, their processes will come to hold or delays occur while damaging the relationship with the suppliers. This will drop the credit rating of the company, the good will be damaged, which will affect when our customers are in the supplier hunting process. Further our employees are stressed out by trying to get down the required materials on time, resulting drop in the quality of service provided to customers. Thus not paying suppliers on time would be a factor affecting 3PL businesses. Hence if we want to get orders and be Economical, Effective & Efficient (3E.s) suppliers to our customers, first we need to be a good customer to our suppliers.

With the globalization things happen in instantaneously. The most successful product or the service of the organization could turn in to a lossmaking product in overnight. Thus customer service is of greater importance and continuous communications with customers has become a hard and fast rule to identify the changes in customer needs & wants in order to meet customer satisfaction. For example customers moving to healthy eating & drinking has made a dramatic effect on the brand "Coca Cola" resulting a drastic loss in the market share of the most profitable drink. However

identifying this change Coca Cola is diversifying to new markets & new products. Thus close communications with suppliers too is an essential fact to identify the supply markets for the items to be procure, the factors affecting the price, capacity, skilled labour. However the main intelligence system to get proper and instantaneous communications and information is the relationships, the business to business relationships (B2B). Thus failure to have proper relationships may result in less communications and less information and be a factor affecting business failure.

Thus it concludes that customer shift to competitor as a component to resources profile variable, Suppliers not paid on time, as a component to financial management profile, strategic business units wise budgets not prepared as a component of strategic management profile, CEO not valuing employees and non availability of training & development as components of administration & HR, less relationship result in less information as a component of customer-supplier relationships are the significance factors affecting business failure in 3PL companies.

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