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Original Article

# Entrepreneurial Business Models for Small and Medium Enterprises (SMEs) from a Perspective of SMEs' Informal Sector in Zambia

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Received: 28 February 2024; Accepted: 30 July 2024; Published: 30 August 2024

**Abstract:** Entrepreneurship and innovation sustainability among small and medium enterprises (SMEs) draws worldwide attention because of the significance of the SMEs in economic development metrics, such as employment creation. However, factors that are attributed for the hindrance of sustainability and entrepreneurial capacity among SMEs remain varied and an open question in both practice and theory. Similarly, though there are possible business models to attain sustainability suggested in theory, these too are varied and remain an open question. This is even more pronounced in developing countries like Zambia. The objective of this study was twofold: to identify the internal and external factors that hinder business growth and sustainability of SME's in the informal sector, and also to propose a model for business growth and sustainability for SMEs. The study adopted a descriptive mixed method approach by the use of both qualitative and quantitative methods. Respondents were selected using convenience sampling, and data collection from 100 SME's selected from 10 markets in Lusaka, Zambia, was by using questionnaires, face-to-face interviews and observations. Findings indicate that there are a number of both internal and external factors that hinder business growth and sustainability of SME's in the informal sectors of retailing and metal fabrication in Lusaka, Zambia. Identified factors included lack of innovation and creativity; lack of a succession plan; lack of consistency and endurance; desire to grow the business fast without due considerations; high interest rates for loans; and lack of access to source capital and poor management of the SME's. The study proposed Business Models based on Stochastic Modelling; and Perren's Framework of Micro Enterprises Model, i.e. Deterministic Approach Model, and the 3P's of sustainability Model of SME's to make SME's business strategy more sustainable and profitable. These proposed models and approaches have potential to lessen the many challenges facing the SMEs which are a mixture of both internal and external factors.

**Keywords:** SME's, SME Business Models, Entrepreneurial Sustainability.

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## 1. Introduction

International experience has shown that SMEs are becoming major contributors to economic growth. In India, SMEs are said to contribute 70% towards Gross Domestic Product (GDP) and to account for over 90% of all industrial units. In Central Asia, Kyrgyzstan, there are 36 SMEs for every 1000 citizens contributing 44% of GDP (MCTI, 2008).

In the case of Zambia, the informal sector and SMEs are the most prolific, sources of employment, wealth creation and a breeding ground for industries. Therefore, the development of SMEs is viewed

as one sustainable way of reducing the levels of poverty and improving the quality of life of households through wealth, job creation and sustainable development (MCTI, 2008). In this regard, the Government of Zambia has formulated and implemented policies which were aimed at creating more business opportunities as well as reducing poverty levels for its citizens. Examples of these policies include the Small Industries Act of 1981, Small Enterprises Development (SED) Act of 1996, The Poverty Reduction Strategy Paper (PRSP) of 2000-2004 (GRZ, 2000), and the Citizens Economic Empowerment Act of 2006, and the Revised National Micro, Small and Medium Enterprise Development Policy of 2023.

However, despite the above interventions and potential to contribute to economic development and wealth creation, the Zambian SMEs appears to have challenges of sustainability. For example, the contribution of retail and metal fabrication sector to the Gross Domestic Product (GDP) for Zambia, has been minimal. 0.4 percent in 2019, -12.6 percent in 2020 and 2.3 percent in 2021 (Bank of Zambia, 2021). And yet the retail and metal fabrication sectors are very cardinal to growth of any economy. Additionally, there is no business model in Zambia that suggests how to achieve sustainability of SME's in the informal sectors of retailing and metal fabrication in Zambia.

Literature indicates that SMEs are faced with specific challenges that hinder their business growth and survival. The development of SMEs is viewed as one sustainable way of reducing the levels of poverty and improving the quality of life of households through wealth, job creation and sustainable development. However, the scenario in the Zambian case is different. Entrepreneurs are still struggling with sustainable of growth and innovation. SMEs are face challenges that hinder their business growth and survival. These challenges are attributed for many Zambian SME's experiencing unsustainable businesses and making them fail to survive longer after being set up (Alfred, 2015).

The above notwithstanding, the factors and possible business models remain open questions in both practice and academics. It is therefore, important to investigate the persistent challenges of low business sustainability of SMEs in the informal sector needs so as to draw out lessons that could be useful for addressing the sustainability challenges faced by SMEs in the informal sector.

## 2.0 Research Objectives

Against the above background, this study was undertaken to investigate the challenges faced by these SMEs in the various markets in the informal sector in Lusaka, Zambia. The specific objectives were:

- (a) To identify the internal and external factors that hinder business sustainability of SME's in the informal sectors of retailing and metal fabrication in Lusaka, Zambia; and
- (b) To propose a model that can lead to business sustainability of SME's in the informal sectors of retailing and metal fabrication in Lusaka, Zambia.

## 2. Literature Review

In literature, the subject of entrepreneurship and sustainability has been approached variously and literally discussions have shown that the nature of the constraints vary from one country to another, suggesting that each country's institutional framework may be the factors behind the varied nature of the constraints.

Some of the prominent discourses around the subject have focused on the considered following themes.

### (a) Categorisation, Description of Role and Types of Entrepreneurs and SMEs

SMEs have been discussed under various categorisations. Discourse in literature have included the following:

- The world changer

The world changer thrives to make the world a better place, and they are going to do whatever they can to make it happen. They understand the concept of society, harmony and empathy and they are fueled by desire to create something that will benefit people's lives.

Before being entrepreneurs, World changers are philanthropists. They do not care about having a particularly lucrative career.

They might create a device to make water drinkable where it is not. They might create a nonprofit to help people in need. Who knows?

One famous world changer is Andrew Carnegie, who expanded the steel industry as well as the American railroad system, changing American society infrastructure and creating tons of jobs in the process. (He was so committed to helping others that he gave 90 percent of his money to charity).

- The Survivor

They are one of the kinds who are sick of the 9-5 and may have had some bad professional experiences in the past. They decided to rebel against the system and take control of their lives. They started their business for freedom and financial independence it entails.

One famous survivor is Jan Koum who migrated to the United States of America from Ukraine with his food stamps. He is now the founder of famous messaging app “What’s App” and is now worth \$6.8 billion.

- **The Visionary**

They think outside the box. In fact, there is no such thing as a box in their world. Visionaries are known for their innovative minds, creativity and ultimate devotion to their ideas.

They are also known for their marketing and branding skills. Like modern gurus, their goal is to preach new ideas and convince people that it will change their lives forever. For many, it is a risky gamble but for some, it works. They become modern icons and superstars like Steven Jobs.

This famous entrepreneur is may be the most famous visionary of all time! He pioneered a series of revolutionary technologies as the founder of Apple, and for years, his brand has been associated with being different and going against the grain.

- **The strategist**

They are walking excel spreadsheets. In fact, the excel spreadsheets are organized in excel spreadsheets. They know everything about their business, there is no angle they haven’t considered or stone they left unturned. They have done their homework, that’s for sure!

Money is their main motivation and their strategic thinking skills and analytical like, Elon Musk, whose shrewd understanding of the auto industry allowed him to create one of the most in-demand products on the market today.

**(b) Characterization of Entrepreneurs**

Some of the characterization used in literature regarding entrepreneurs have five featured common elements as follows:

- **Passion.** A startup founder is often driven by the quest for deeper purpose beyond the sheer mechanics of operating a business. If an entrepreneur has the passion for his/her startup, it will drive him/her to turn his/her idea into reality.
- **Perseverance.** Entrepreneurs need to be able to deal with obstacles. A business is not built overnight, and turning your idea into a reality will take time. Follow –up is key. People might present plenty of excuses for not getting back in touch with you. Yet if you show, persist in trying to make things happen, one will probably succeed.
- **Resourcefulness.** A vital ability for an entrepreneur is to make the most of what you have. Your assets as an entrepreneur will be limited, so use them to the fullest.
- **Open-Mindedness.** As an entrepreneur, you may think you have zeroed in on a business plan, but you will need to learn to take in the opinions of others. If your plan fails to work, then adjust.

**(c) Gender and Small Business Growth**

Tundui (2015) examined gender and small business growth in Tanzania by conducting a survey to 310 owner- managers of SMEs. The study highlighted financial capital and access to loans as having on positive impact on male growth aspiration in the case of Tanzania.

**(d) Internal and External Factors Influencing SME Performance**

Grimsholme and Poblete (2019) examined internal and external factors hampering SMEs growth, using qualitative approach. Among the internal factors, entrepreneurial knowledge, education of employees, marketing, technology and innovation are among these factors. In addition, the level of education of entrepreneurs themselves are considered necessary in equipping them with knowledge and skills needed to effectively manage and succeed in businesses (Storey, 2015). According to Morrison (2019) internal factors emanate within an organization due to management and company organization characteristics. Factors that are frequently considered as part of the internal environment include the marketing objectives, human resource strategies such as employee motivation, staff turnover and provision of training, leadership styles, investment in R&D and its organizational culture. Others include entrepreneurial skill. The majority of the establishments in the informal sector lack capacity building programs, hence, they often employ people with low skills base. Due to financial constraints, SMEs tend to spend less on training than large Enterprises (Tannock et al, 2020). Further, it is argued that the quality of management is essential for organization business opportunities. However, in many developing countries the quality of the management is low (Bruhn, 2019). Studies concluded that education equips people with knowledge and skills they need to effectively manage and succeed in their businesses. That is, as the level of increases the Entrepreneur skills an individual entrepreneur’s ability to cope with problems and take hold of opportunities that are important to the growth of the firm also increase (Storey, 2015).

In Zambia, the Small Business Policy identifies several internal constraints to SMEs growth including, inadequate market information, inadequate resources for extension services, lack of competent management and human capability and inadequate of qualified personnel (GRZ, 2000).

As for external factors, it is argued that these constraints emanate outside the firms due to activities of other agents in the markets such as suppliers, customers, competitors, and the government. The government influences the functioning of the markets through laws, rules, and regulations. Therefore,

these are the institutional frameworks that constraints the behaviors of firms. For example, trade regulation, labor regulation, public procurement procedures, business licensing and taxes. Efficient institutional frameworks enable firms to flourish, whereas inefficient institutional frameworks increase transaction costs and, hence, erodes profits and discourage investment by the enterprises (World Bank, 2019). Grimsholme and Poblete (2019) found the major obstacles faced by SMEs included lack of access to finance, competition, barriers to trade, management competence, lack of skilled labour, low investment in R&D and new technology. Access to finance is considered a critical problem for small and medium firms compared to large sized-firms (Hughes and Storey, 2015). The majority of small firm's private investment comes from domestic sources (Sinha and Fiestas 2011).

Zambia, like in many developing countries, financial market and institutions are less developed. Hence, firms encounter limited financial support for long term financing. Most banks in Lusaka mostly provide short term loans with high interest rate (SMEs Development Policy, 2019). Financial banks have to charge higher interest to finance small enterprises.

In Kosovo, a study examining the factors influencing SMEs growth using a qualitative method of interviews and observing 200 entrepreneurs found that financial support, law and regulations, business location, competition, globalization, management and employment competence factors had effect on firm growth (Soini and Veseli, 2015). Others have suggested that good government policy resulted into an improvement in the business environment for domestic business to grow (Naudé and Krugell, 2019). Further, excessively high rates of tax exert high cost in terms of lower private investment and growth. Taxes reduce the incentive to invest. Djankov et al. (2019) found that corporate tax rate has a large adverse impact on aggregate investment and entrepreneurial activity. Therefore, unfavorable government regulations can be a serious constraint to SMEs growth.

#### **(e) Other Constraints**

Some discourses have considered and highlighted some constraints and factors in isolation. For example, market constraints have been considered in many forms. In Zambia, for example, the geographical size of Lusaka offers a limited market growth. However, while firms can utilize the market outside Lusaka such as Tanzania and across the borders of East African community to sell their products. Yet, entrepreneurs encounter difficulties in entering into these markets and other world markets (MLYW, 2017; Brush *et al.*, 2019). One argument according to Mhede (2015) is that insufficient marketing information on buyer and suppliers, and poor market infrastructure affect SMEs growth.

In terms of Government constrains, it can be argued that firms need to be regulated and licensed. However, if the costs they incur in complying with regulation are unnecessarily high, business entry and firm growth will be lower. Regulations impose necessary costs on firms such as the need to adapt the business to meet regulatory requirements or to pay licensing fees. But too often these costs are unnecessarily high because of rent seeking behavior, inefficient administration, or poor institutional fit (World Bank, 2019a). The effects of regulatory barriers and business licensing on firms' dynamics therefore reduce business entry and firm growth (Djankov, 2019).

All the common strands of literature notwithstanding, studies in the context of Zambia have not delved on some of the vexing questions, namely:

- (a) The relationship between internal constraints that SMEs encounter such as lack of entrepreneurial business skills and growth;
- (b) Relationship between external constraints that SMEs encounter such as lack of access to finance, lack of access to market information, and unfavorable Government regulation and growth.

It is worth noting that prior studies have shown that the rate of challenges in developing countries is higher than in the developed world, (World Bank, 2007). Scholars have indicated that starting a business is a risky venture and warn that the chances of small scale business owners making it past the five-year mark are very slim in the conditions of developing countries. Hence the importance of undertaking the current study.

### **3. Materials and Methods**

This research used a descriptive study aimed at developing an entrepreneurial innovation business model as a determinant factor for small and medium enterprises sustainability in the informal sector. The focus was to develop a model for SMEs sustainability and growth with focus on both the internal and external business factors. The study identified Deterministic Approach Model which is based on the fact that internal and external factors can be identified to explain growth of SMEs.

Therefore, the study used both quantitative and qualitative types of research. The main population of the study was 457 traders in these markets of whom 257 were retail traders and 200 were metal fabricators. A non-probability sampling method was applied in order to pick the 100 respondents

regardless of the gender, age, or race to avoid biases. Each respondent was given an equal chance of being included in the sample.

This study was conducted in Lusaka's ten community market areas, namely, Chaisa Market, Chelston Market, Chawama Market, Mtendere Market, Garden (Mwasauka), Kalingalinga Market, Kabanana Market, Kazimayi market, Mandevu Market and Soweto Market. Data was collected between December 2022 and February 2023. Questionnaires and interview guides were the main instruments used for collection of data in this research. Face-to-face interviews with respondents were used to gain responses on the factors both internal and external that impact the sustainability of SMEs in Lusaka. These too were supplemented by observations by the researcher.

### 3. Results and Discussion

The key findings of the study were as follows:

- (a) From the research conducted, it was evident that lack of business sustainability of new SMEs is very high. This negatively impacts on the ability of new SMEs to contribute meaningfully to job creation, economic growth and more equal income distribution. SMEs find it difficult to expand their businesses because of these internal and external factors. Operational stability and expansion in business require external sources of finance by way of working capital to attend to intermittent cash flow deficits and investment capital to purchase fixed assets to facilitate expansion.
- (b) The study also revealed that the business environment was not too enabling. In order of intensity, the financial constraints, market constraints, human capital and infrastructure constitute the greatest challenges faced by SME's. Financial constraints were in form of inaccessible start-up capital, working capital, investment capital, high interest rates, foreign exchange rates volatility, and poor customer repayments. These were followed by market constraints which was as a result of unfair competition from imports selling cheaply as a result of subsidies and having too many competitors.
- (c) Another key finding was that of low educational levels and suitable skills among most of the workers resulting in low productivity and poor product quality was quite evident. Other constraints included lack of affordable business premises and land, and health problems related to HIV/AIDS constituted other constraints for SMEs in the study area.
- (d) There is inadequate business information in Lusaka district. The Government of Republic of Zambia, through the Ministry of Small Medium Enterprises Development (MSME) should work in collaboration with the Zambia Development Agency so as to organize seminars and business drills for these SMEs.

**Table 1 Availability of required information**

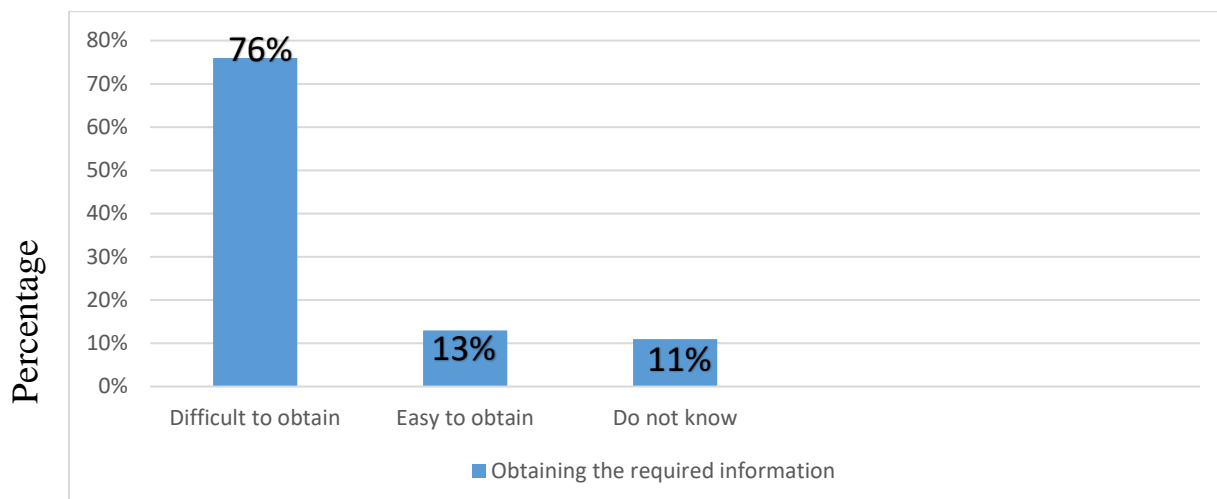
Responses	Frequency	Percentage
Readily Available	13	13%
Moderately Available	24	24%
Not Available	63	63%
Total	100	100%

**Source: Field data, 2022**

Table 1 shows availability of the required information by the enterprises was. Thirteen percent responded that information required was readily available. Twenty four percent indicated that the information was moderately available. Sixty three percent indicated that the required information was not available.

**Table 2 How to obtain the required information**





**Table 3. Obtaining the information required**

Figure 3 shows how easy or difficult it is in obtaining the required information. Seventy six percent indicated that it was difficult to obtain the required information. Thirteen percent indicated that it was easy to obtain the required information for the enterprise. Eleven indicated that they did not know.

- (e) The study found out that most SMEs prefer to use personal savings and contributions from relatives because they find it very difficult to access financing from commercial banks due to strict requirements such as collateral security and high repayment costs. The study therefore recommends that banks and other credit giving financial institutions should come up with creative policies that make it easy for the SMEs to access financing.

**Table 4. Sources of funding**

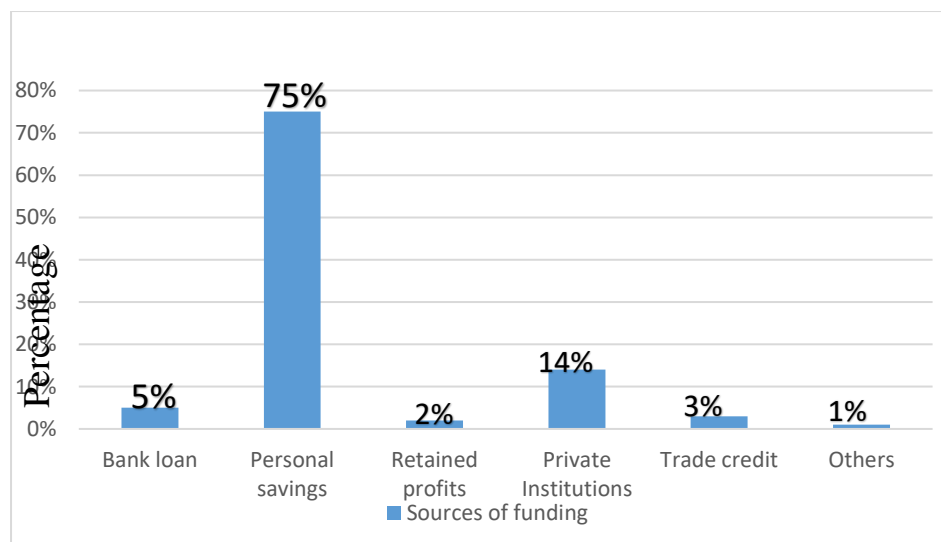


Table 4 shows the source of funding for the businesses. Five percent of respondents indicated that they had obtained a Bank Loan. Seventy five percent of respondents indicated that it was from their personal savings. Two percent of respondents indicated that it was from the retained profits. Fourteen percent of respondents indicated that they got it from private institutions. Three percent of respondents indicated that they got it from trade credits and One percent indicated other reason other than those given above. SMEs also fail due to a lack of capital. King (2007:15) states “lack of capital is often the most critical challenge that a successful SME faces as its very success creates this and it quickly becomes a vicious circle.” Without cash flow, management and/or raising more capital, including debt, the business is often constrained by capital as it grows. Often, the profit in one operating cycle is insufficient to fund the extra working capital required for the next operating cycle. This is especially the case where a business is either inventory or receivables intensive and/or the operating cycle is a long one (i.e. the operating cycle is the average time that it takes from the first receipt of inventory to when the customer pays for the goods). This can be exacerbated when capital goods are required to process the goods and the company cannot finance the acquisition of these capital assets. Many SMEs cannot overcome the obstacles in their businesses cash flow cycle and cannot understand why bankers and other lenders often cannot provide the financing, as SMEs often do not have the security to support the debt.

**Table 5. Source of capital for the Business**

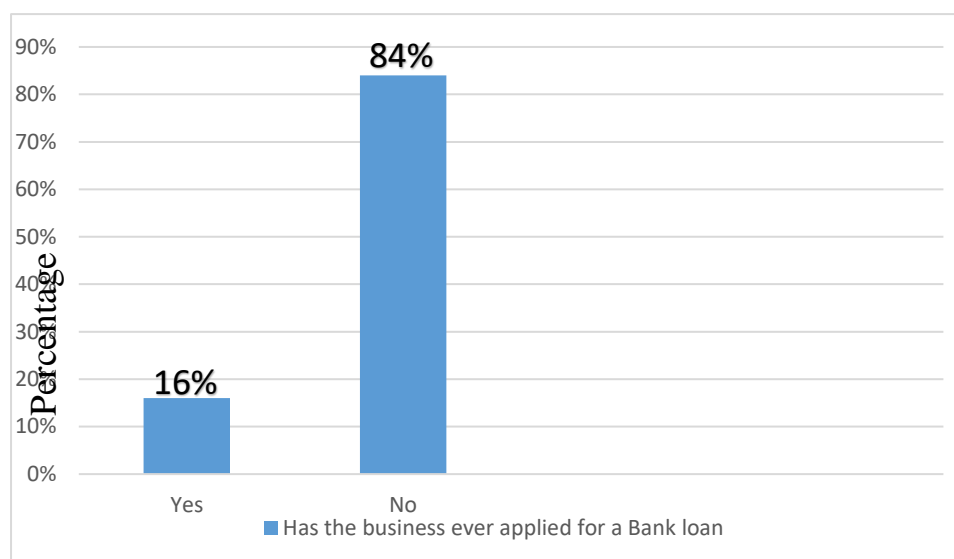


Table 5 reveals the figures of the respondents who had applied for a Bank Loan. Sixteen percent indicated that they had applied for a Bank Loan whilst Eighty four indicated that they had never applied for a bank loan.

**Table 6 Relationship with the bank**

Responses	Frequency	Percentage
Excellent	3	18.75 %
Good	6	37.50 %
Average	5	31.25 %
Poor	2	12.50 %
Total	16	6

Table 6 shows the responses of the sixteen respondents who had obtained a bank loan and their relationship with their bankers. Three respondents indicated that their relationship was excellent. Six respondents indicated that their relationship was good. Five respondents indicated that their relationship was average with two stating that their relationship was poor.

#### 4. Conclusions

Some of the interventions to enhance the capacity of SMEs include:

- Policy Review, Development and Implementation: Developing cross cutting but stand-alone National Policy on SMEs be established as a matter of urgency, especially with a new Ministry now created the Ministry of Small and Medium Enterprises.
- Policy Level Capacity Building for SMEs: The Government could work in collaboration with various government and non-government actors in designing and implementation of various capacity building initiatives for the SMEs, based on need-assessments.
- Financing Incentives: Access to finance is another factor to be considered. Such should include policy incentives to encourage financial institutions to revisit their loan regulations so as to provide services to small business enterprises.
- Hardware and Software Infrastructure: Access to infrastructure affects the growth of SMEs only to a moderate extent. The study recommends renovations of public goods such roads, electricity power and water challenges.
- Information Accessibility: Policy makers should consider how they might play a role in facilitating networks where SMEs can share and learn from each other. Encouraging business expos and symposia.

#### 5. Areas for further research.

Arising from this study, the following directions for future research should be carried out. This research only covered micro and small enterprises Lusaka district from the informal sector. However, there are other enterprises that are medium and large firms in the same district, from the formal sector. Researchers are

encouraged to research on them. In future, other SMEs in other towns should be involved to enable the researcher to make adequate conclusions.

This research didn't concern itself with the challenges and possible solutions hindering SMEs from accessing financing by credit giving institutions. In future, a research should be instituted to establish the challenges and the possible solutions.

Further, in future, a comparison should be done between the financial performance of SMEs that have received microcredit and the ones that have not received the financing. This will help in shedding more light on whether accessing microcredit helps the SMEs to perform better.

**Author Contributions:** The author confirms sole responsibility for the following: study conception and design, data collection, analysis and interpretation of results, and manuscript preparation.

**Funding:** This research received no external funding.

**Acknowledgments:** The author thanks Africa Research University for approving their study as this is an extract from a PhD Thesis.

**Conflicts of Interest:** The authors declare no conflicts of interest.

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