Financial Management and Profitability among Small and Medium Enterprises (SMEs) in Uganda

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Abstract:-**The study was carried out to examine the role of financial management on profitability among SMEs in Uganda. The data was collected from 200 respondents from selected SMEs in western Uganda. The study employed a descriptive correlation and cross sectional survey design. SPSS was used in data analysis. Regression analysis was also used to determine the effect of equity and debt financing on the components of performance which were profitability. Pearson's Correlation Coefficient was used to establish the relationship between variables and to draw the conclusion on the hypothesis. The study revealed that that working capital management has a significant effect on profitability, internal control has significant effect on profitability in SMEs and that that there is a positive significant relationship between financial management and profitability in SMEs in Uganda, The study recommended that owners and managers of SMEs should improve on the management of working capital through reducing the level of inventory and credit collection from customers and that staff which is independent from those responsible for the system, such as the internal auditor, should provide additional assurance on the effectiveness and cost efficiency of the internal control system**

Key words: **Financial management, Profitability, SMEs profitability**

I. INTRODUCTION

Like any other part of the country in Uganda, failure of SMEs in western Uganda is not an exception. Financial management analysis forms an area of concern to the owners of SMEs most especially if the attainment of business goals is constrained Padachi K (2006). Poor business performance has for long remained unexplained most especially in the third-world countries perspective where the Small and Medium Enterprises occupy the large part of the economy Garcia-Teruel (2007). However, some studies from developed nations (Nguyen, 2001) cite inefficient financial management practices to contribute immensely to SMEs poor business performance.

Theoretical Review:

The study was guided by the Knowledge-based theory propounded by Grant (2002). The theory states that knowledge is an important resource which SMEs owner-mangers can use to boost their performance. The knowledge-based theory of the firm considers knowledge as the most strategically significant resource of a firm. Its proponents argue that because knowledge-based resources are usually difficult to imitate and socially complex, heterogeneous knowledge bases and capabilities among firms are the major determinants of sustained competitive advantage and superior corporate performance (Wernerfelt 1984, Barney 1991, Conner 1991).

II. REVIEW OF RELATED LITERATURE

Effects of working capital management on SME profitability

Working Capital Management (WCM) practices have an effect on companies' profitability (Peel Wilson, 1996; Agyei-Mensah, 2010) because it affects firm risk and profitability (Smith and Sell, 1980). For Small and Medium Enterprises (SMEs), there is the need for particular attention to the control and monitoring of Working Capital because of their higher proportion of current assets, less liquidity, volatile cash flows and reliance on short-term debt relative to large firms (Peel et al., 2000; Howorth and Westhead, 2003). However, evidence suggests that few SMEs employ formal WCM practices but instead rely on ad hoc or subjective WCM decisions (Khoury et al., 1999, Howorth and Westhead, 2003), although Perren and Grant (2000) suggest that the lack of formalization with SMEs does not necessarily imply poor firm control. The WCM practices of firms are very important because it determines the level of working capital available, which intends influences profitability.

According to Peel and Wilson (1994), there are factors that differentiate the WCM practices between SMEs and larger firms including: (1) SMEs have the tendency of great reliance on Credit management and bank overdrafts for short-term financing, (2) a willingness on the part of SMEs to grant over-generous credit terms to obtain business, particularly from larger companies, (3) relatively weak control procedures in SMEs and (4) lack of clear policy on WCM by SMEs. Likewise, Atrill (2006) also identified factors that distinguish the WCM practices of SMEs and larger companies including: (1) SMEs lack of appropriate resources to manage WCM and (2) lack of market power by SMEs.

According to Martinez-Solano, (2007); Raheman and Nasr, (2007) WCM practices importance to profitability is potentially useful for the management of SMEs who have limited resources, including management competency (Small Business Research Centre, 1992; Gockel and Akoena, 2002; Pansiri and Temtime, 2008) and equipment and technology (Abor and Quartey, 2010; Saleh and Ndubisi, 2006; Berisha-Namani, 2009) and need to prioritise deployment of resources to a particular practice in order to maximise profitability (Tauringana and Afrifa, 2013).

The first research that comprehensively surveyed the working capital practices of companies was conducted in 1978 by Smith and Sell (1980) in the United States (US). In their research they used a survey instrument consisting of 35 questions. Out of a sample of 653 industrial firms, 210 usable responses were received representing a 32.2 per cent response rate. They concluded that WCM in practice is far more than just a series of independent technologies. Belt and Smith (1992) also conducted a research into the working capital practices in US with a sample of 448 largest industrial companies. With a questionnaire of 38 questions, they received 105 usable responses representing a 23.4 per cent response rate. Using longitudinal data of a ten-year period, they suggested a pattern of more formality and sophistication in how current assets and liabilities are managed in practice. A research into the WCM practices of SMEs in Canada, US and Australia was also conducted by Koury et al. (1998). They used a sample of 350 firms randomly chosen from ten industries within the BOSS database and received a 57 usable responses representing a 15.8 per cent response rate. The findings found that only 7 per cent of Canadian SMEs have formal working capital policies.

Nyamao et al. (2012) conducted a study to elucidate the WCM practices of SMEs in Kenya using a sample of 113 SMEs. They concluded that WCM practices are low amongst SMEs as majority had not adopted formal WCM routines. Agyei-Mensah (2010) also conducted a research into the WCM practices of SMEs in the Ashanti region of Ghana. Using a sample of 800 randomly selected firms the study revealed weak WCM skills within the sector.

Despite the importance of WCM to SMEs, a research by Burns and Walker (1991) and Peel and Wilson (1994) show that only 24 per cent and 20 per cent respectively of the financial managers time is spent on working capital. Harif et al. (2010) did a research on the financial management practices of SMEs in Malaysia, with the results indicating that lack of working capital which accounted for 93.6 per cent is the most common weakness in the area of financial management.

Cash management

Is the management of the cash balances of a concern in such a manner as to maximize the availability of cash not invested in fixed assets or inventories and to avoid the risk of insolvency. According to Keynes there are three motives for holding cash: the transactions motive, the precautionary motive, and the speculative motive. The most useful technique of cash management is the cash budget

Cash management is a broad term that refers to the collection, concentration, and disbursement of cash. The goal is to manage the cash balances of an enterprise in such away as to maximize the availability of cash not invested in fixed assets or inventories and to do so in such a way as to avoid the risk of insolvency. Factors monitored as a part of cash management include a company's level of liquidity, its management of cash balances, and its short-term investment strategies. (Springer, 2005]

Cash management is a broad term that refers to the collection, concentration, and disbursement of cash. It encompasses a company's level of liquidity, its management of cash balance, and its short-term investment strategies. In some ways, managing cash flow is the most important job of business managers. If at any time a company fails to pay an obligation when it is due because of the lack of cash, the company is insolvent. Insolvency is the primary reason firms go bankrupt. Obviously, the prospect of such a direction sequence should compel companies to manage their cash with care. Moreover, efficient cash management means more than just preventing bankruptcy. It improves the profitability and reduces the risk to which the firm is exposed.

According to Remenyi (2001), the purpose of literature review was to establish the area of study, establish a the idea put forward by Palom (2001) and indicating that it might be possible to encourage debtors to pay more quickly by offering discounts for earlier payment. In order to improve cash management efficiency and enable more availability of cash the company can use this as an alternative solution. The objective of managing accounts receivable is to collect accounts receivable as quickly as possible without losing sales from high pressure collection techniques (Gitman, 2008).

Cash management: Davidson (1992) defined cash management as a term which refers to the collection concentration and disbursement of cash. It encompasses a company’s level of liquidity, management of cash balance and short term strategies. Pindado (2004) also defines cash management as part of working capital that makes up the optimal level needed by a company. Bort (2004) noted that, cash management is of importance for both new and growing businesses. Companies may suffer from cash flow problems because of lack of margin of safety in case of anticipated expenses such that they experience problems in finding the funds for innovation or expansion. Weak cash flow makes it difficult to hire and retain good employees (Beranek, 2000)

According Ross (2000) said that, it is only natural that major business expenses are incurred in the production of goods or the provision of services. In most cases, a business incurs such expenses before the corresponding payment is received from customers. In addition, employee salaries and other expenses drain considerable funds from most business. These make effective cash management an essential part of the business financial planning. According to Bort (2004) cash is the lifeblood of the business. The key to successful cash management lies in tabulating realistic projections, monitoring collections and disbursements, establishing effective billing and collection measures, and adhering to budgetary parameters because cash flow can be a problem to the business organization.

Cash collections: According to Ross (2000), cash collection is a function of accounts receivable, it is the recovery of cash

from a business or individual with which the company is issued an invoice. Gitman (2008) and Vanhorne (2001), offer theoretical positions drawn from their observations and consulting experience on the fact that a firm can improve its cash management efficiency by collecting accounts receivable as soon as possible. The most obvious way of bringing forward cash inflows, would be to press debtors for earlier payment although this policy resulted in goodwill and problems with customers (Palom,2001). There was very little scope for speeding up payments when the credit period currently allowed to debtors is no more than the norm for the industry. Myers (2004)defend the idea put forward by Palom (2001) and indicating that it might be possible to encourage debtors to pay more quickly by offering discounts for earlier payment. In order to improve cash management efficiency and enable more availability of cash the company can use this as an alternative solution. The objective of managing accounts receivable is to collect accounts receivable as quickly as possible without losing sales from high pressure collection techniques (Gitman, 2008).

Credit management

Wilson (1996) found in a research conducted in the United Kingdom that good credit management practices have connection with company profitability. Berryman (1983) also concluded that poor or careless WCM is a major cause of SME failure. The WCM practices of SMEs are different from their larger counterparts because of their unequal access to finance (Tauringana and Afrifa, 2013). However, the advocates in finance literature seem to be focused on larger companies. Javis et al. (1996) interviewed 20 SMEs and indicated that 'best practice' models advocated by finance literature are not necessarily appropriate to SMEs and that alternative approaches may be viable. SMEs due to their smallness may be in a weaker position in terms of their dealings with suppliers and customers. As argued by Solanki (2009), SMEs cannot command suppliers' credit in the way large firms do and also if they remain slow payees the supplier may refuse credit or they may quote higher prices. Research shows that WCM practices in SMEs are inadequate (Poutziouris et al., 2005).

Emery (1987) focuses on Credit management as an operational tool, addressing the role of uncertain product demand in a firm's operating decisions. As demand fluctuates, sellers face two alternatives: either they can allow the selling price to fluctuate so that the market always clears, or they can vary production to match demand. Either option is quite costly. If price varies, potential buyers face extremely high costs of information search. If production varies, sellers face extremely high production costs. Credit management could help to smooth irregular demand through stimulating sales by relaxing Credit management terms in slack demand periods (Emery 1984, 1988; Nadiri, 1969). The operational motive predicts that firms with variable demand extend significantly more Credit management than firms with stable demand. Long et al. (1993) find empirical evidence that is consistent with this view. We test the effect of Credit management under uncertain product demand conditions on firm profitability. Following the operational motive, we expect the profitability of receivables held by firms with high sales uncertainty to be higher than that held by firms with sales certainty.

A commercial perspective, Nadiri (1969) argues that availability of alternative payment terms can expand the market by increasing product demand. According to the commercial motive, Credit management improves product marketability by facilitating firm's sales. So, for firms with less market share (less market power) Credit management should prove more beneficial, as these firms have stronger incentives to increase sales (Hill et al., 2010). Hill et al. (2010) find that the profitability of receivables is a decreasing function of market share. However, market pressures might force small business with no market power to offer normal industry credit terms, regardless of its possible negative impact on profitability. We test the effect of Credit management on profitability for less market presence firms and for firms with high market share.

Emery's paper (1984) is based on information costs. Capital market imperfections require selling firms to maintain adequate liquid reserves that they either can invest in marketable securities or lend out through trade credit. Imperfections also allow seller firms to acquire knowledge about customers' ability to pay at a relatively low cost. This creates an informational advantage over third party intermediaries and allows sellers to offer Credit management at an implicit interest rate that is lower than the purchaser could obtain elsewhere. In this sense, Emery (1984) argues that suppliers may extend credit if the implicit rate of return1 earned on receivables exceeds that of other investments.

Petersen and Rajan (1994) and Atanasova (2007) show that implicit returns earned from Credit management are typically large, relative to feasible opportunity costs. The Emery model (1984) suggests that more liquid firms will extend Credit management as an alternative to investing in marketable securities. In the same vein, Ng et al. (1999) argue that Credit management is given from firms with high liquidity to firms with low liquidity. Consequently, we expect that more liquid firms secure a higher return on investment in trade credit.

Schwartz (1974) developed the financial motive for the use of trade credit. He suggests that when credit is tight, financially stable firms will increasingly offer more Credit management to maintain their relations with smaller customers, who are "rationed" from direct credit market participation. The seller firm acts as a financial intermediary to customers with limited access to capital markets, financing their customers' growth. Petersen and Rajan (1997) find empirical evidence that firms with better access to capital markets offer more trade credit. Larger firms are thought to be better known and have better access to capital markets than smaller firms, in terms of availability and cost, and should therefore face fewer constraints when raising capital to finance their investments

(Faulkender and Wang, 2006). Financial motive predicts a positive connection between extending Credit management and firm size according to which, creditworthy firms should extend Credit management to less creditworthy firms (Emery, 1984; Mian and Smith, 1992; Schwartz, 1974). According to the financial motive of trade credit, we expect a greater effect of Credit management on firm profitability for the subsample of larger firms.

Inventory management

Inventory management is the process of efficiently overseeing the constant flow of units into and out of an existing inventory. This process usually involves controlling the transfer in of units in order to prevent the inventory from becoming too high, or dwindling to levels that could put the operation of the company into jeopardy. Competent inventory management also seeks to control the costs associated with the inventory, both from the perspective of the total value of the goods included and the tax burden generated by the cumulative value of the inventory.

Balancing the various tasks of inventory management means paying attention to three key aspects of any inventory, the first aspect has to do with time. In terms of materials acquired for inclusion in the total inventory, this means understanding how long it takes for a supplier to process an order and execute a delivery. Inventory management also demands that a solid understanding of how long it will take for those materials to transfer out of the inventory be established. Knowing these two important lead times makes it possible to know when to place an order and how many units must be ordered to keep production running smoothly.

Maintaining optimal inventory levels reduces the cost of possible interruptions and prevents loss of business arising from scarcity of products. It also reduces supply costs and protects against price fluctuations. Setting the right inventory holding period is the main goal of inventory management. A study to investigate the optimal inventory levels was carried out by Swaminathan (2001), found out that adjusting raw materials and finished goods as a component of inventory is faster than the inventory as a whole to reach the reasonable levels. Autukaite and Molay (2011) found out that there are some other methods that can ease inventory management such as order quantity method and just-in-time inventories. Empirical studies have shown that inventory conversion period has a negative effect on a business's performance. For instance, shortening the inventory conversion period could increase stock out costs of inventory which results in losing sales opportunities and leads to poor performance (Deloof, 2003). Managers of firms should therefore keep their inventory to an optimum level since mismanagement of inventory will lead to tying up excess capital at the expense of profitable operations (Lazaridis and Dimitrios, 2005). Lazaridis and Dimitrios, further points out that too much inventory could demand more physical space, could lead to a financial distress, and increases the possibility of inventories damages, deterioration and losses. Moreover, holding large amount of inventory frequently indicates inefficient and careless management practices and procedures. On the other hand, too little inventories might lead to the interruption of operation in manufacturing, increase the possibility of losing sales and consequently lower the profitability of the firms.

Singh (2008) studied the relationship between inventory management and working capital management focusing on the importance of inventory management. He found out that firms with a poor inventory management can cause serious problems which destroy the long-term profitability and firms' survival chances. Also firms with well-thought inventory management can reduce the inventory to an optimal level which has no negative effect on production and sales. The study also indicates that the size of inventory directly affects the working capital and its management.

The effect of internal control systems on profitability of SMES in Uganda

Internal control is an essential prerequisite for effective and efficient management of any organization. Most of the SMEs lack the proper system of internal control which results in various fraudulent activities. It has become the core objective of management to implement an effective internal control system appropriate to the nature and size of the entity. Benefits of an internal control system include effectiveness and efficiency of operations, reliability of financial reporting and compliance with applicable laws and regulations(Webster, 1991).

SMEs have concentrated on the availability, accessibility and cost efficiency in the utilization of finances. Little attention has been paid to the great role played by the internal control systems in the performance of businesses. Small and medium scale enterprises have operated in total disregard of internal control systems leading to the mass failure of these business organizations (Were, 2011). Studies show that 90% of the business start-ups do not operate beyond the third anniversary due to lack of sound internal control systems.

Anduuru (2005) points out the importance of internal control systems. He notes that the external auditors find it difficult to rely on internal control systems of small and medium scale enterprises. This is so because such business entities have not established elaborate systems of internal controls, there is no adequate segregation of duties and there are no assurances as to the completeness of recording business transactions. Ongoing monitoring activities of small entities are more likely to be informal and typically performed as part of the overall management of the entity's operations (Wamae, 2005). Management's close involvement in operations often will identify significant variances from expectations and inaccuracies in financial data leading to corrective action to the controls.

Wolf (1994) argues that basic concepts of the entity's risk assessment process are relevant to every entity, regardless of

the size, but the risk assessment process is likely to be less structured in small entities than in larger, well established entities. Weber (1998) points out that small entities may implement the control environment elements differently than larger entities. Small entities might not have written codes of conduct. Moreover, those charged with governance in small entities may not include an independent or outside member. Small entities are less committed to the advancement or hiring of qualified personnel to positions of responsibility in business entities.

Small scale enterprises are mostly managed by family members and close relatives who show less interest in following internal control systems they have to the latter. Internal controls are a function of internal audit function (Messier, 1997). Small entities have disregarded this important function whose benefits may prove to be more than the costs of having none. Messier (1997) points out that a firm's performance depends heavily on a sound internal audit function. Small and medium sized businesses are not too small for effective internal controls (Putra, 2011). Even a relatively small business can enforce certain internal controls that are very effective. To have a competitive edge over the rest of the firms, business entities constantly carry out appraisals of their internal control systems. Therefore, the basis of superior enterprise financial performance is stronger, reliable and up to date systems of internal controls

Relationship between Financial management practices and profitability in SMEs

Concerning the relationships between working capital management practices and SME profitability, Abdul Raheman et al., (2007) provide some relevant findings as follows: Profitable firms reviewed their working capital policies on monthly and quarterly bases; profitable firms used an ROI (return on investment) criterion in looking at changes in the management of certain working capital components; profitable firms always or sometimes take discounts on payables whereas aggressive firms and those with written working capital policies were net users of trade credit. Some theoretical researchers do indicate the relation- ships between financial management and profitability. Filbeck et al. (2000) indicated that there is a relationship between liquidity and profitability. The study done by Garcia-Teruel et al, (2007) entitled "effects of working capital management on SME profit- ability in Spain" found a significant negative association between working capital management and SME profitability. In variance to the findings of Garcia-Terel (2007), the results from the study conducted by Uyar (2009) indicate significant positive correlations between working capital components with firm's performance in Malaysia.

According to Bhunia et al. (2012) liquidity has a significant impact on profitability. However, such studies in Uganda are scanty and more over, literature available in developed nations see (MacMahon, 1998, Nguyen, 2001, Peel et al., 1996) looked at individual constructs of financial management majorly like working capital management.

Mathuva (2009) examined the influence of working capital management components on corporate profit- ability by using a sample of 30 firms listed on the Nairobi Stock Exchange (NSE) for the periods 1993 to 2008. The findings from his study revealed that there exists a highly significant negative relationship between the time it takes for firms to collect cash from their customers.

The results also revealed that there exists a highly significant positive relationship between the period taken to convert inventories into sales (the inventory conversion period) and profitability, and there exists a highly significant positive relationship between the time it takes the firm to pay its creditors and profitability. The same results coincides with Uyar (2009) results which showed statistical significant between working capital and firm performance.

Collis (2002) reported a positive correlation between structure of accounting department and profitability of business. In Uganda, majority of the SMEs owners do not consider book keeping necessary (Lois and Annette, 2005). Whereas there are some SMEs that prepare reports, they keep incomplete records which do not give a clear picture of the financial position and profitability of the firm (Ernst and Young, 2011).

Czarnitzki and Hottenrott (2011) analyzed the relationship between working capital management and profitability of small and medium-sized enterprises in Germany by controlling for unobservable heterogeneity and possible endogeneity. The authors examined a non-linear relation between these two variables and have shown that there is a non-monotonic (concave) relationship between working capital level and firm profitability, which indicates that SMEs have an optimal working capital level that maximizes their profitability. Profitability is one of the most important objectives of financial management because one goal of financial management is to maximize the owner's wealth (McMahon, 1995). Thus, profitability is very important in determining the success or failure of a business. At the establishment stage, a business may not be profitable because of investment and expenses for establishing the business. When the business becomes mature, profits have to be produced.

III. METHODOLOGY

The study being a survey, it adopted correlational and cross-sectional designs. The correlational design was used because the study involved relating two variables Financial Management and Profitability. The cross-sectional design allowed the obtaining of useful data in a relatively short period of time. The sample comprised 200 SMEs staff of selected branches in Western Uganda. The study employed simple random sampling a technique by which the respondents were selected at random and entirely by chance. The sampling method gave every member of the SMEs staff

an equal chance of being included in the sample enabling collection of data that produced findings that can be generalized. The researchers personally collected data and ensured that the study was carried out in an ethical manner. Ethical issues given utmost importance by the researchers were obtaining informed consent from the respondents, guaranteeing anonymity, confidentiality, respect for privacy and ensuring honesty in the presentation, analysis and interpretation of the results by strictly basing them on the data collected.

Instrument: Using the quantitative approach, particularly the survey design, data were collected using a self administered questionnaire (SAQ). The SAQ comprised of background characteristics of the respondents with nominal questions on the respondent's gender, age, marital status, educational level, experience in service and qualifications as well as position in the company. Content validity index (CVI) was measured by ensuring that the questions or items in questionnaire conform to the study's conceptualization . In order to test the Reliability of the tool, pilot test was used to test their internal consistence. (Amin 2004). The questions were based on the five-point Likert scale from a minimum of 1 for the worst case scenario (strongly disagree) to a maximum of 5, which is the best case scenario (Strongly agree).

Data Management: Data analysis in this study was done with the help of SPSS (Statistical Package for Social Sciences software package). This package helped in establishment of findings through, frequencies, percentages and means. Regression analysis was also used to determine the effect of equity and debt financing on the components of performance which were profitability. Pearson's Correlation Coefficient was used to establish the relationship between variables and to draw the conclusion on the hypothesis. Considering Retrieval rate, since all respondents did not return the questionnaire, it was important to determine the rate of the questionnaires that were returned against those that were distributed. The retrieval rate was 96% and the researcher considered it as appropriate to base on those questionnaires returned for analysis and generalization of findings

IV. RESULTS

The study had the demographic characteristics of the respondents that were observed and presented in the table of frequencies.

Table 1: Demographic Characteristics of Respondents

(n=192)

Gender	**Frequency**	**Percentage (%)**
Male	100	52.1
Female	92	47.9
Total	192	100
Age of Respondents		
18-20	5	3
21-25	15	8
26-30	25	13
31-35	46	24
36-40	67	35
41-45	26	14
46-50	8	4
50+ and above	-	-
Total	192	100
Position in the company		
Owner Manager	102	53.1
Hired Manager	90	46.9
Total	192	100
Educational Level		
Post graduate	10	5
Bachelor	20	10
Diploma	53	28
Secondary	65	34
Primary	44	23
Total	192	100
Marital status		
Single	32	17
Married	138	72
Divorced	8	4
Widowed	14	7
Total	192	100

The findings revealed that majority of the respondents were male with 52.1% implying that most people who own or run the SMEs are male, Females taking only 47.9%.The age of respondents indicates that 3% are in between the age of 18-20 years old, 8% were in the age between 21-25years old, 13% were in the age between 26-30years old, 24% were in the age between 31-35years old, 35% were in the age between 36-40years old, 14% were in the age between 41-45years old, and also 4% were in the age between 46-50years old respectively. Indicating that almost all kinds of the different aged groups participated and provided their respondents in the data collection;

The proportions of the respondent to their Position in the company are shown in the table as the Majority were Owner Manager with 53.1% and Hired Manager 46.9% respectively. Implying that most SMEs are ran by owners. The education level of respondents indicates that bachelor's degree holders were 10%, Diplomas holders were 28%, Secondary level were the majority with 34% and those with Primary level were 23% respectively. Besides to this about 72% of the respondents were married, 17% were single while on the other hand, divorced were 4% and windowed were 7% respectively.

Table 2: Descriptive statistics on working capital management

	Inventory management	**Mean**	**Interpretation**
	Inventory is kept safely with appropriate security	2.75	High
	You record all the inventory on annual	3.25	High
	You always plan the inventory levels in your business	3.23	High
	Average mean	**3.08**	**High**
	Credit management		
	You have provided your customers with alternative means of paying their accounts	3.23	High
	You collect money from customers in the acceptable time period	2.96	High
	You only grant credit to customers after accessing their credit worthiness	2.89	High
	Customers do not take long to clear their accounts	3.23	High
	You always pay your creditors when they fall due	3.40	Very high
	Average	**3.14**	**High**
	Cash management		
	You have a control system for cash	3.30	Very High
	You bank all the cash sales every day	2.58	High
	You have a cash policy for your business	3.25	High
	You have a safe where you keep your cash for safety	2.65	High
	No single person is responsible for authorization and approval before cash is paid out.	3.40	Very High
	Average	**3.04**	**High**

Working capital management was broken down into inventory management, credit management, and cash management. All these sub variables were found to have high average mean values; inventory management (3.08); credit management (3.14); and cash management (3.04) respectively. This implies that most respondents agreed with the statements which provided in the questionnaire.

Table 3 Descriptive statistics on internal control (n=192)

	Internal controls	Mean	Interpretation
1	Your business has internal control systems	3.23	High
2	Necessary procedures are taken when paying out cash	3.96	Very high
3	Necessary procedures are taken when requisitioning for materials	2.89	High
4	Different people are required to handle different tasks for a specific transaction	3.36	High
5	Credit policies are well established and always followed	2.55	High
	Checks and balances are put in place for employees to follow	3.23	High
	Average mean	3.20	High

Results showed that the interpretation of the means reveal the mean values are high implying that most respondents agreed with the statements provided in the questionnaire. Results further show that necessary procedures are taken when paying out cash with a mean value of 3.96 being the highest mean value.

Table 4 Descriptive statistics on profitability

Results on profitability as a dependent variable were analyzed through descriptive analysis using mean values.

Descriptive statistics on profitability (n=192)

	Profitability	**Mean**	**Interpretation**
1	You always meet the targeted revenue	2.55	High
2	You are able to meet your financial obligations as they fall due	2.75	High
3	Your sales have been increasing in the previous periods	2.55	High
4	You incur minimal costs to carry out your business functions	2.62	High
5	Your business has appropriate capital employed to run it.	2.45	Low
	Average mean	**2.58**	**High**

Source Primary data 2016

Through descriptive analysis by use of means, the results showed that most respondents agreed with the statements in the questionnaire because of the high average mean value of (2.58)

Table 5 Regression results showing effect of working capital on profitability

	Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	
1	.564[a]	.318	.290	.84603	
	a. Predictors: (Constant), Cash mgt, inventory mgt, credit mgt				
	ANOVA[a]				
Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	24.414	3	8.138	11.370	.000[b]
Residual	52.251	186	.716		
Total	76.665	189			
a.	b. Dependent Variable: Profitability c. Predictors: (Constant), Cash mgt, inventory mgt, credit mgt				
	Coefficients[a]				
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig
		B	Std. Error	Beta		
1	(Constant)	.663	.626		1.059	.293
	Cash mgt	.107	.209	.078	.512	.610
	Inventory mgt	.504	.209	.337	2.413	.018
	Credit mgt	.259	.194	1.337	1.337	.185
	a. Dependent Variable: Profitability					

Findings revealed that working capital management has significant effect on profitability in SMEs in Western Uganda. From the ANOVA results indicated that the sig value is (0.000<0.050). The r^2 value =0.318, this means the working capital management affects profitability of SMEs by 31.8%. However, these results further imply that the effect is a weak, because on observation the effect is less than 50% and this is also evidenced by the low values of the F- statistic and t-statistic respectively. To get better results in (profitability), it is important to put in mind the constructs considered in this study. This is true because considering only one of them may not have significant effect on profitability. This is supported by the coefficients of each of the constructs.

Table 6: Regression results showing effect of internal control on profitability

	Model Summary					
Model	R	R Square		Adjusted R Square	Std. Error of the Estimate	
1	.496[a]	.246		.237	.86909	
	a. Predictors: (Constant), Internal control					
	ANOVA[a]					
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	19.022	1	19.022	25.184	.000
	Residual	58.160	188	.755		
	Total	77.182	191			
a.	b. Dependent Variable: Profitability c. Predictors: (Constant), Internal control					
	Coefficients[a]					
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig
		B	Std. Error	Beta		
1	(Constant)	1.797	.482	.496	3.731	.000
	Internal control	.611	.122		5.018	.000
	a. Dependent Variable: Profitability					

Results from table 4.6 reveal that internal control has significant effect on profitability in SMEs in Western Uganda with (sig value = 0.000<0.05). Findings further indicate that r^2 = 0.246, meaning that internal control has 24.6% effect on profitability of SMEs in Western Uganda. As indicated with low values of F and t statistics, the findings mean a weak effet.

Table 7. Correlation between financial management and profitability

		FM	Profitability
FM	Pearson Correlation	1	.667
	Sig. (2-tailed)		.000
	N	192	192
Profitability	Pearson Correlation	.667	1
	Sig. (2-tailed)	.000	
	N	192	192

Results indicated that there is a positive significant relationship between financial management and profitability. Result shows the sig value = 0.000 < 0.001. This implies that profitability is strongly associated with how finances are managed. This further may mean that if finances are well managed, profits in SMEs can increase. It was hypothesized that there is no relationship between financial management and profitability in SMEs in Western Uganda. However, the study found that financial management had a significant relationship with profitability. Person's correlation coefficient was 0.667 and sig value was 0.000, implying a positive significant relationship. Therefore rejecting the null hypothesis and accepting the alternative hypothesis.

V. DISCUSSION

Effect of working capital management on profitability

Findings from the study revealed that working capital management has a significant effect on profitability. These results are in line with Raheman and Nasr (2007) who studied the effect of different variables of working capital management on profitability and found a significantly positive association between size and profitability. Further, Mathuva (2009) examined the influence of working capital management components on corporate profitability of 30 Kenyan listed firms. The study finds a significantly negative relationship between accounts collection days and profitability, a significantly positive association between inventory conversion period and profitability and a significantly positive relationship between average payment days and profitability. The findings of this study therefore confirm the traditional view of efficient working capital management and its effects on profitability. Martinez-Solano (2007) investigated the effects of working capital management on the profitability of a sample of small and medium-sized Spanish firms. Their findings revealed that managers can create value by reducing their inventories and the number of days for which their accounts are outstanding. Moreover, shortening the cash conversion cycle may improve the business profitability.

Effect of internal control on profitability in SMEs

Results in this study reveal that internal control has significant effect on profitability in SMEs in Western Uganda This is line with Beeler et al, 1999) who observed that internal control are associated with lower revenues, which explore links between disclosure of material weakness and fraud, earnings management or restatements Internal controls provide an independent appraisal of the quality of managerial performance in carrying out assigned responsibilities for better revenue generation. Further Fadzil et al (2005) observe that an effective internal control system unequivocally correlates with organizational success in meeting its revenue target level. Effective internal control for revenue generation involves; regular a review of the reliability and integrity of financial and operating information, a review of the controls employed to safeguard assets, an assessment of employees' compliance with management policies, procedures and applicable laws and regulations, an evaluation of the efficiency and effectiveness with which management achieves its organizational

The relationship between financial management and profitability among SMEs

Findings indicate that there is a positive significant relationship between financial management and profitability. Other scholars have found similar findings; Deloof (2003) found out that the way working capital is managed will have a significant impact on the profitability of a firm. Padachi (2006) investigated the relationship between profitability measured by return on assets and working capital management. The regression result showed that high investment in inventories and receivables is associated with low profitability. Gill, et al (2010) also studied 88 American firms and found out statistical significant relationship between cash conversion cycle and profitability.

VI. CONCLUSION

Basing on the discussion above, it was concluded that working capital management has a significant effect on

profitability in small and medium enterprises in Western Uganda and Efficiency in managing working capital enhances profitability, Internal controls have positive significant effect on profitability of small and medium enterprises and there is a strong positive relationship between financial management and profitability in small and medium enterprises. The null hypothesis of no relationship between financial management and profitability is rejected and the alternative hypothesis is accepted, that financial management has significant positive relationship with profitability in small and medium enterprises in Western Uganda. The study recommended that Owners and managers of SMEs should improve on the management of working capital through reducing the level of inventory and credit collection from customers.

Secondary, staff that is sufficiently independent from those responsible for the system, such as the internal auditor, should provide additional assurance on the effectiveness and cost efficiency of the internal control system.

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