Status of Profitability of MSMEs in a Developing Country: Uganda as a Case Study

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Abstract

The study set out to assess the status of profitability of MSMEs in Uganda. A cross sectional descriptive design in which both qualitative and quantitative approaches were used was adopted to study a sample of 371 respondents who were systematically sampled from four districts of Wakiso, Mukono, Kampala and Jinja. Most respondents disagreed (65.7%) that their MSMEs are profitable although some significant number of respondents (32.0%) stated that their MSMEs are profitable. Only 2.2% were not decided on the profitability status of their MSMEs. Most MSMEs are not profitable and one of the major problems is poor utilisation of assets and equity to produce return. It is recommended that for profitability to be achieved and consequently growth, the MSMEs should critically examine proposals to purchase assets while recognizing the business they are doing. They should separate for instance business assets and personal assets while making purchasing decisions for business vehicles. Efforts should be made such that whenever equity is contributed, return is made thereon. There should not be additional capital from owners that does not earn a return. Instead efficiency is needed with operations to ensure that operations are profitable so as to increase return on capital invested in form of equity funds.

Key words: Business; Earnings; Equity; Firms; Gross profit; Net profit; Profitability; MSMEs.

1. Introduction

In Uganda the generally adopted concept of MSMEs is stratification on the basis of number of employees and turnover.

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Those employing between one to four people with a turnover of up to ten million Uganda shillings ($0 to approximately $2,500) are categorised as micro. Those employing between five to forty nine people with a turnover between ten and one hundred million (approximately between $2,500 and $25,000) are categorised as small. Those with between fifty and one hundred employees and a turnover between one hundred and three hundred and sixty million Uganda shillings (approximately between $25,000 and $90,000) are categorised as medium. [1] In Uganda 80% of the MSMEs are located in urban and semi-urban centers. Their activities span a continuum ranging from service provision, selling of goods, information technology, agriculture and furniture making among others. MSMEs are crucial in the development of economies worldwide. They are spread across all sectors with 49% in service sector, 33% in commerce and trade, 10% in manufacturing and 8% in others. The relevance of MSMEs in the economic development and growth of African GDP is highlighted in the employment figures in Nigeria, South Africa, and East African countries [2].

2. Literature Review

Between 70-80% of MSMEs in Africa are micro and very small enterprise, while medium enterprises account for between 5-15%. They provide the main source of jobs and income in the continent. African women entrepreneurs own more than half of the micro and small enterprises. They play an increasing role in diversifying production and represent 70% of the active population in rural areas [3]. Contribution of MSMEs to GDP vary greatly among and between countries. Their contribution to employment ranges from as low as 15% in Zimbabwe to 90% in Ethiopia and as regards contribution to GDP it is as high as 70% in Ghana [4]. The global collective effort geared towards transforming the livelihoods of the several billions of underprivileged peoples of the world are perhaps best evidenced through the Sustainable Development Goals (SDGs). These target the promotion of inclusive and sustainable economic growth, providing employment and decent work for all, promoting sustainable industrialisation and fostering innovation, and reducing income inequalities. MSMEs are key players in the economy and the wider eco-system of firms. Thus, enabling them to adapt and thrive in a more open environment and participate more actively in the digital transformation is essential for boosting economic growth and delivering a more inclusive globalisation [5].

2.1 MSMEs and Employment

MSMEs play a very important role and provide a viable option for employment and job creation, especially for the billions of youth worldwide. This is so regardless of whether a country is developed emergent or poor. In recognition of this reality, the Government of Uganda has embarked on the promotion of youth self-employment by establishing the National Youth Funds and the Youth Venture Capital Fund (UYVCF) established in 2011. In 2013, the Youth Livelihood Programme (YLP), worth about US$ 100 million, was initiated to run over a five-year period [6]. Such support is required from government, development partners and apex organisations if the MSMEs are to survive and grow. This is in line with the two major propositions, namely, enabling policies and targeted interventions, which are necessary for MSME growth. This is achieved through networking [7]. At the global level, it has been observed that nine out of ten new jobs worldwide are created by small businesses. Nearly 3.3 million jobs will be needed every month in emerging markets by 2030 to absorb the growing workforce. Both the private and public sector can better address this problem if they have better insights about
the magnitude and nature of the finance gap to be met. Conservative estimates put this at about $2 trillion annually. Others are more staggering, indicating 65 million enterprises, or 40 percent of formal micro, small and medium businesses in developing countries, to have an unmet financing need of $5.2 trillion every year [8].

2.2 MSMEs Mortality rate and survival

MSMEs in Uganda are predominantly informal and young. About 50% of them are less than five years old. Mortality rate of businesses is high and for every new business being established, another is closed within one year of its operation. In Uganda only about 8% of the MSME enterprises have been around for 15 years or more [9]. Evidently, these important vehicles for economic and social transformation face challenges to their sustained survival and growth. In fact, even the transition to medium scale is uncommon. Most SMEs remain small scale. Most business failures of MSMEs in the final analysis, reflect a lack of profitability [10]. Relative to big businesses, small ones are disproportionately disadvantaged. Formalising their existence and high compliance costs exacerbate the resource and cash-flow constraints. A valid registration certificate and a trading license are normally major requirements for accessing resources from outside, be it trade credit or finance. A Tax Identification Number (TIN) as well as an account in a commercial bank on a list in the databank of government agencies or international institutions and Non-Government Organisations (NGOs) may be prequalification requirements for submitting bids for lucrative contracts. These requirements may be a deterrent to formalisation.

2.3 Profitability

Profitability or monetary performance embodies quantifying the outcome of a business’s entire operations in terms of money. In order to gauge a firm’s profitability diverse alternatives key financial ratios can be employed, for example, earnings per share, net profit ratio, gross profit ratio, return on equity, assets and capital employed. There are various definitions for each of these and other ratios [11]. Various factors impact on the profitability of a firm, directly or indirectly. Some do so very strongly, such as cost of goods sold, interest rate, tax rate and inventory volume. The profitability of firms can be gauged through a number of financial ratios [12]. All businesses have some kind of capital which may be contributed wholly contributed by the owner or external funders or a combination of both sources. For MSMEs, much of the time the owner(s) contributes all or a very big proportion of the funding. Conventional analysis of the contribution of capital to profitability of firms dwelled more on how long term investment affect profitability. Little attention was given to the management of the daily income and expenditure of the firms affects its profitability. There was very little research on how working capital management affects the profitability [13]. Ratio analysis is about comparative relation between figures. In the case of businesses this may be to establish a trend in the relationships over periods of time. It may also relate businesses of comparable sizes. It has been observed that return on assets has a positive impact on profitability, for example, a reduction in the average collection period will lead to an increase in profitability and it is therefore important for excess cash receivables to be reinvested in the short run so that it can generate more cash inflow and thus increase profits [14].

2.3.1 Measuring Profitability
There are various approaches to appreciating the profitability of firm, some of which are, by way of ratios, return on Sales (net profit margin), return on total assets (ROTA), return on capital employed (ROCE), return on equity (ROE), and earnings per share((EPS).

2.3.2 Return on Sales (Net Profit Margin) Ratio

This ratio measures the profits after taxes on the year's sales. The higher this ratio, the better prepared the business is to handle downtrends brought on by adverse conditions. It is given by the formula: (Earnings after tax/Total sales) x 100. The return on sales may also be measured by Gross Profit Margin Ratio. This ratio measures the percentage of gross profits on the year's sales. The higher the ratio, the better prepared the business is to handle downtrends brought on by adverse conditions. It is given by the formula: (Gross profit /Total sales) x 100

2.3.3 Return on Total Assets (ROTA) Ratio

This ratio shows the after tax earnings of total assets and is an indicator of how profitable a company is. Return on assets ratio is the key indicator of the profitability of a company. It matches net profits after taxes with the assets used to earn such profits. A high percentage rate will tell you the company is well run and has a healthy return on assets. It is given by the formula: (Earnings after tax/Total Assets) x 100

2.3.4

Return on Capital employed measures the ability of a company's management to realize an adequate return on assets belonging to owners in the company. It is given by the formula: (Earnings after tax/Net Assets) x 100.

2.3.5

Return on Equity or return on average common equity, return on net worth, return on ordinary shareholders’ funds) (equity) measures the rate of return on the ownership interest or shareholder’s equity. It measures a firm's efficiency at generating profits from every unit of shareholders' equity (also known as net assets or assets minus liabilities). ROE shows how well a company uses investment funds to generate earnings growth.

2.3.6

Earnings per share refers to the portion of a company's profit allocated to each outstanding share of common stock. Earnings per share serve as an indicator of a company's profitability. EPS is calculated as:

\[
\text{Net Income - Dividends on Preferred Stock} \\
\text{Average Outstanding Shares}
\]

When calculating, it is more accurate to use a weighted average number of shares outstanding over the reporting term, because the number of shares outstanding can change over time. However, some authors simplify the
calculation by using the number of shares outstanding at the end of the period. Diluted EPS expands on basic EPS by including the shares of convertibles or warrants outstanding in the outstanding shares number. Globally, the status of profitability of the MSMEs is closely linked to the market share determined by the concentration of these MSMEs or the market structure. The structure–conduct–performance (SCP) paradigm that dominated Industrial organization (IO) until the early 1980s holds that market structure (the number of and size distribution of firms in an industry) determines market conduct (the way in which the firms in that industry interact), which in turn determines firm performance (profitability). Proponents of the paradigm claim that market structure is principally influenced by technological factors such as economies of scale and scope, and that the existence of high profit levels in an industry is evidence that the firms in that industry possess monopoly power. Typically, they regress average profit rates on a number of market–wide variables such as indices of horizontal concentration, measures of economies of scale and other barriers to entry, R&D and advertising intensities. Generally, the profitability of MSMEs is moderate given high levels of industry concentration. In Uganda, it is not clear what the level of industrial concentration is, but the level of profitability is hypothesized to be determined by many factors this study was bound to disclose. Profitability *perse* may not be a good indicator of a business enterprise’s financial health Another approach to assessing a firm is as indicated in the table below.

### Table 1: How to determine profitability in MSMEs

<table>
<thead>
<tr>
<th>Determinant factor</th>
<th>Formula</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tangible assets ratio</td>
<td>Tangible Assets/Total Assets</td>
<td>Tangible assets include both fixed assets such as machinery, buildings and land, and current assets like inventory property</td>
</tr>
<tr>
<td>Growth opportunities Ratios</td>
<td>Price Earnings ratio: Share price /Earnings per share Market Business Ratio: Market Value of a firm/Business Value of firm</td>
<td>The company’s growth opportunities are measured by market indicators such as price to book value (PBV), or price earnings ratio (PER).</td>
</tr>
<tr>
<td>Solvency ratio</td>
<td>Long term debt/ Equity</td>
<td>Creditworthiness determines constraints on cash management and hence a decrease in profitability.</td>
</tr>
<tr>
<td>Current asset turnover ratio</td>
<td>Current assets /revenues</td>
<td>On how many days are valued current assets into cash.</td>
</tr>
<tr>
<td>Coverage of Interest ratio</td>
<td>Coverage of interest ratio: EBIT/Interest charges</td>
<td>This indicator shows how often debt costs may be covered by operating activities of the SME. This indicator is directly linked to profitability, a great value will have to lead to high profitability</td>
</tr>
</tbody>
</table>

Source: Bagh (2016)

Although break-even or even loss may be tolerated in the short run, making profit is a major motive of every business organisation. Sustained earnings per share, with its corollary of shareholder wealth maximisation, cannot be achieved without profit. A business that repeatedly incurs losses is candidate for not being a going concern. Profit also enables a business to access funds at minimal cost and enables it avoid restrictive covenants associated with borrowing [15]. This is not to argue that only equity or retained earnings have to be used to
finance a business, because external funding in line with the pecking order theory has some benefits such as a tax shield. When optimally leveraged, a business may attain a profitable position. In a research carried out regarding the average collection period it was noted that its reduction led to an increase in profitability of the firm. It is therefore important for excess cash receivables to be reinvested in the short run so that it can generate more cash inflow and thus increase profits. There are endogenous factors that impact on the profitability, some being macroeconomic factors. Research reveals that the macroeconomic factor, such as interest and tax rates can be key determinants of whether a firm makes profit or incurs loss [16]. A study on profitability of micro firms revealed that firm size, growth of sales, lagged profits, productivities, asset turnover and firm’s age were key variables that affect profitability [17].

3. Justification of the Study

The purpose of the study was to examine the status of liquidity management of MSMEs in Uganda. While liberalization of the economy that commenced in early 1990s was intended to promote profitability and growth of private enterprises including MSMEs, most of them have not registered any substantial amount of profit. This has presumably negatively impacted on their growth. Hitherto there appears to be no substantial evidence of research specifically on the status of profitability of MSMEs in Uganda. Study results may lend a hand to policy makers and MSME managers and owners while formulating policy guidelines to enhance profitability of MSMEs, hence their survival and growth. It is also intended to complement existing literature on profitability of MSMEs for future researchers and academicians [18].

4. Methodology

In this section the researcher analyses the research design, area of study, study population, selection of the sample, data sources, research tools and methods, methods that were used for testing validity and reliability of research findings, research procedure and data analysis techniques that were adopted on the study.

4.1 Research design

The study adopted a descriptive design in which both qualitative and quantitative approaches were used. The quantitative approach is concerned with trying to quantify things; it asks questions such as ‘how long’, ‘how many’ or ‘the degree to which’ and it was aimed at quantifying data and generalising results from the sample of the population. It was used to measure the incidence of various views and opinions in the sample or aggregate results. The quantitative element of the study included the use of frequencies, percentages, means correlations and regressions to arrive at conclusions. On the other hand, the qualitative approach attempted to enable the researcher gain an understanding of the underlying reasons and motivations for actions and to establish how people interpreted their experiences. It provided insights into the setting of a problem and in generating ideas. The qualitative nature of the research was aimed at clarifying the results of the quantitative approach through descriptions, discussions, conclusions and recommendations [19].

4.2 Area of study and study population
The study sampled the districts of Wakiso, Mukono, Kampala and Jinja. These are the districts with the majority of MSMEs in the country and their impact is not only sheer number of MSMEs but also on the amount of turnover which they generate and the number of employees. It is estimated that 65% of the about one million MSMEs in Uganda are located in these districts. Hence the study population was composed of 650,000 MSMEs. Thus, picking samples of MSMEs from these districts was hypothesized to help make deductive conclusions on other MSMEs in other locations. These districts were purposively selected.

4.3 Sample size and selection method

A sample of 400 respondents was arrived at using the formula for large populations [21]. This is stated as follows:

\[ n = \frac{pq}{(SE)^2} \]

Where

- \( n \) is the sample size
- \( p \) is the proportion of the population possessing the major attribute
- \( q = 1 - p \)
- \( SE \) is the standard error of the proportion.

For large populations whose proportion of the population possessing the attribute is unknown, the confidence interval should be set at 5% and the confidence level at 95% and compute the SE as follows:

\[ SE = \frac{5\%}{1.96}, \text{ where } 1.96 = \frac{z}{\sqrt{2}} \]

also known as the critical value, the positive \( z \) value that is at the vertical boundary for the area of \( \frac{p}{2} \) in the right tail of the standard normal distribution

This implies the SE =0.025. Note that when one cannot estimate the population, one sets \( p \) at 0.5.

This further implies that \( n = (0.5)(0.5)/(0.025)^2 = 400 \).

Sample selection from each district was systematically done as follows:

Both primary and secondary sources of data were employed in the study. Primary source consisted of the respondents sampled from MSMEs while secondary data consisted of textbooks, journals, magazines, newsletters and other publications. The former provided first hand information relating to study variables while the later provided information that could not be captured from primary sources.
Table 2: The sample selection per district

<table>
<thead>
<tr>
<th>District</th>
<th>No of MSMEs</th>
<th>Number of respondents from each MSME</th>
<th>Total Number of respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jinja</td>
<td>50</td>
<td>2</td>
<td>100</td>
</tr>
<tr>
<td>Kampala</td>
<td>50</td>
<td>2</td>
<td>100</td>
</tr>
<tr>
<td>Mukono</td>
<td>50</td>
<td>2</td>
<td>100</td>
</tr>
<tr>
<td>Wakiso</td>
<td>50</td>
<td>2</td>
<td>100</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>200</strong></td>
<td></td>
<td><strong>400</strong></td>
</tr>
</tbody>
</table>

Sources of data

4.4 Research Tools and Methods

Both close and open-ended questionnaires were used to solicit responses from respondents. The close-ended questions enhanced precision and conciseness while open-ended questions helped to clarify the responses provided in close-ended questionnaires. The questionnaires were self-administered and this enhanced response through clarification of the questions especially to respondents that could not read and write. The use of self-administered questionnaires also justifies the neglect of interview guide since interviews were held with respondents as the questionnaires are being administered. To enhance data analysis, a uniform rating scale (the 5-point Likert scale) was adopted in preparation of questionnaires. In this, the following codes were defined as follows: 5 denoted strongly agree, 4 denoted agree, 3 denoted undecided, 2 denoted disagree while 1 denoted strongly disagree.

4.5 Validity and Reliability

Validity determines whether the research truly measures what it is intended to measure or how truthful the research results are. To ensure validity in research, examination of trustworthiness is crucial. The trustworthiness of a research report lies at the heart of issues conventionally discussed as validity and reliability” [22]. To ensure validity of research instruments, the researcher constructed instruments that were used to solicit data from the sample of respondents. Content validity index (CVI) was used to establish validity of the instruments [23]. Thus:

Content validity index (CVI) =

\[
\text{Sum of agreement on every relevant judgment x 100}
\]

Total number of items (questions)

Using the formula, the results which were obtained and recommendations were incorporated and validity re-determined until an appropriate index is achieved, and this is put at above 75%. The resultant CVI was 95.7% implying that the contents in the research instruments were valid in relation to study variables. Reliability refers
to the level of dependability of the questions in the research instrument [24]. Testing for internal consistency is needed to ensure this dependability and this has been done using the Cronbach alpha coefficient (α)[25].

\[
\alpha = \frac{K}{K-1} \left(1 - \sum \frac{SD^2_i}{\sum SD^2_t}\right)
\]

Where \( \alpha \) = Alpha coefficient

\( K \) = Number of items in the instrument

\( \sum \) = Summation sign

\( SD^2_i \) = Standard deviation squared within each item

\( SD^2_t \) = Total Standard deviation

The resultant coefficient should be above 0.75 if the contents of the instruments are to be considered reliable as asserted by Cronbach. Test statistics revealed alpha coefficient of 0.824 implying internal consistency in the scaling of items, hence reliability of the study instruments.

4.6 Procedure

The researcher requested permission from the organisations’ management and made contacts with the respondents. Instruments were then developed, pilot tested and data collected. Data was analysed and the final report written.

4.7 Data analysis

Both quantitative and qualitative data were used. Quantitative data was processed using the statistical package for social scientists (SPSS) to come out with the necessary frequencies, percentages, graphs and other descriptives. Analysis of Variance (ANOVA), Chi- square and regression analysis were used to test the difference between means and the relationship between the dependent and multiple independent variables while Pearson correlation coefficient was used to test the significance of the relationship between two variables. Qualitative data was thematically analysed to make inferences from what was stated by respondents. These inferences were later integrated with quantitative findings to arrive at relevant conclusions.

4.8 Study Limitations

The study sample was large and located in different, spread far and wide. This posed a challenge in collecting data and finish the study in time. This made research slow and costly. Furthermore libraries were not well stocked with latest text books that would provide a hand in gathering related literature. However, the researcher improved literature review with information from electronic journal articles on the internet although most of the
best articles required subscription that raised the budget from what had been anticipated. Finally, there was a lot of hesitation from the respondents as to the purpose of the information required. It was explained to them that the data and information provided were purely for academic purposes and they were promised confidentiality regarding the information elicited from them. That way a reasonable level of response was achieved.

5. Findings

The status of profitability was assessed using major profitably indicators that included return on sales, gross profit margin, return on assets, return on equity and earnings per share. The questions were whether MSMEs are profitable and this was tested using the second question to help assess the profitability using the above indictors. Regarding the general profitability, the following scale was adopted 5 for strongly agree, 4 for agree, 3 for undecided, 2 for disagree and 1 for strongly disagree. Respondents revealed the following results: Results in table 3 show that most respondents disagreed (65.7%) that their MSMEs are profitable although some significant number of respondents (32.0%) stated that their MSMEs are profitable. Only 2.2% were not decided on the profitability status of their MSMEs. Generally, it can be hypothesized from the results that MSMEs are not profitable given that a larger number (65.7%) stated so. Descriptive statistics were obtained for each of the predictor variables regarding their level as a measure of profitability.

<table>
<thead>
<tr>
<th></th>
<th>Frequency</th>
<th>Percent</th>
<th>Valid Percent</th>
<th>Cumulative Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valid</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strongly Disagree</td>
<td>35</td>
<td>9.4</td>
<td>9.4</td>
<td>9.4</td>
</tr>
<tr>
<td>Disagree</td>
<td>209</td>
<td>56.3</td>
<td>56.3</td>
<td>65.7</td>
</tr>
<tr>
<td>Undecided</td>
<td>8</td>
<td>2.2</td>
<td>2.2</td>
<td>67.9</td>
</tr>
<tr>
<td>Agree</td>
<td>68</td>
<td>18.3</td>
<td>18.3</td>
<td>86.2</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>51</td>
<td>13.7</td>
<td>13.7</td>
<td>100.0</td>
</tr>
<tr>
<td>Total</td>
<td>371</td>
<td>100.0</td>
<td>100.0</td>
<td></td>
</tr>
</tbody>
</table>

Source: Field data

Table 4: Descriptive statistics on the level of predictors of profitability of MSMEs

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>On average, our firm enjoys a high net profit margin</td>
<td>371</td>
<td>1</td>
<td>5</td>
<td>2.20</td>
<td>1.217</td>
</tr>
<tr>
<td>On average, our firm enjoys a high gross profit margin</td>
<td>371</td>
<td>1</td>
<td>5</td>
<td>2.19</td>
<td>1.251</td>
</tr>
<tr>
<td>On average, our firm enjoys a high return on assets</td>
<td>371</td>
<td>1</td>
<td>5</td>
<td>2.33</td>
<td>1.403</td>
</tr>
<tr>
<td>On average, our firm enjoys a high return on equity</td>
<td>371</td>
<td>2</td>
<td>5</td>
<td>2.10</td>
<td>.936</td>
</tr>
</tbody>
</table>

Valid N (listwise): 371
Source: Field data

Results in table 4 show that most respondents on average disagreed their MSMEs enjoy a high net profit margin with mean response at 2.20, while they also disagreed that their MSMEs enjoys a high gross profit margin with mean response at 2.19. Results further indicate that most respondents disagreed that MSMEs enjoy a high return on assets with mean response at 2.33 while they also disagreed that MSMEs enjoy a high return on equity as indicated by the mean response at 2.10.

To investigate the effect of the predictor variables on the dependent variable, profitability, regression analysis was conducted with results presented below.

Table 5: Model Summary of the effect of predictor variables on profitability of MSMEs

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.460(a)</td>
<td>.212</td>
<td>.201</td>
<td>1.128</td>
</tr>
</tbody>
</table>

a Predictors: (Constant), On average, our firm enjoys a high return on equity, On average, our firm enjoys a high net profit margin, On average, our firm enjoys a high gross profit margin, On average, our firm enjoys a high return on assets, On average, our firm enjoys a high return on sales.

The first R is the multiple correlation coefficient existing between all the predictor variables and the dependent variable. This value is 0.460 which indicates that there is a variance shared by the independent variables and the dependent variable. The second value, R-Square, is simply the squared value of R which is used to explain the goodness of fit or the amount of variance explained by the given predictor variables. This value is 0.212 which indicates that 21.2% of the variance in the profitability of SMEs is explained by return on equity, net profit margin, gross profit margin and return on assets.

Table 6: ANOVA table showing the overall variance accounted for in the model ANOVA(b)

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression</td>
<td>124.676</td>
<td>5</td>
<td>24.935</td>
<td>19.602</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>464.300</td>
<td>365</td>
<td>1.272</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>588.976</td>
<td>370</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a Predictors: (Constant), On average, our firm enjoys a high return on equity, On average, our firm enjoys a high net profit margin, On average, our firm enjoys a high gross profit margin, On average, our firm enjoys a high return on assets, On average, our firm enjoys a high return on sales.

b Dependent Variable: PROFITABILITY OF MSMEs

In table 6 are ANOVA results that describe the overall variance accounted for in the model. The F-statistic represents a test of null hypothesis that the expected values of regression coefficients are equal to each other and
that they are equal to zero or whether the R square proportion of variance in the dependent variable accounted for by predictors is zero. However, the larger F- Value (19.602) and small significance level (P<0.05) show that the three predictors are not equal to each other and could be used to predict the dependent variable, that is, the profitability of SMEs.

Table 7: Standard Regression table showing the effect of each individual Predictor Variable Coefficients (a)

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>4.110</td>
</tr>
<tr>
<td></td>
<td>On average, our firm enjoys a high net profit margin</td>
<td>.162</td>
</tr>
<tr>
<td></td>
<td>On average, our firm enjoys a high gross profit margin</td>
<td>.037</td>
</tr>
<tr>
<td></td>
<td>On average, our firm enjoys a high return on assets</td>
<td>-.383</td>
</tr>
<tr>
<td></td>
<td>On average, our firm enjoys a high return on equity</td>
<td>-.332</td>
</tr>
</tbody>
</table>

a Dependent Variable: PROFITABILITY OF MSMEs

In table 7 the standardized beta coefficients for the four predictor variables indicate that return on assets is the best predictor of the profitability of MSMEs (-.426) followed by return on equity (-.246), then net profit margin (0.157) and lastly gross profit margin at (0.036). This is logical because, whether a firm’s assets are totally financed by owners or partly from external sources, it is necessary to ensure that the return thereto is adequate. Low returns are a motivation to investors as well as to external funders. Thus the importance of ratios such as profit before interest and tax and interest coverage, to establish the level of leverage, and impliedly the going concern status of the firm.

6. Conclusion

Study results indicate that most respondents on average disagreed their MSMEs enjoy either high net profit margin or a high gross profit margin. Results further indicate that most respondents disagreed that MSMEs either a high return on assets or a high return on equity. In relation to profitability, MSMEs need to optimally manage assets capacity, for example, by minimising idle assets so as to increase their contribution to the firms’ return. For profitability to be achieved and consequently growth, the SMEs should critically examine proposals to purchase assets commensurate with the business they are doing. For example, they should separate business assets from personal assets such as in the case of vehicles. Additionally, equity should be employed to earn a return. There should not be additional capital from owner’s that does not earn a return. Instead efficiency is needed with operations to ensure that operations are profitable so as to increase return on capital invested in
form of equity funds.

7. Recommendations

Given that there may be factors other than purely financial impacting on the profitability of MSMEs, it is recommended that other researchers pick interest in studying them. Identifying these and weighing their contribution to the profitability and growth may help MSMEs managers and policy makers in making decisions that would enhance profitability, and coincidentally survival and growth in these sectors. For example, other than purely financial factors, conventional business analysis has as a basis, the PESTEL (political, economic, social-cultural, ecological and legal factors) model to plan and predict business success or failure. This especially important given the crucial roles MSMEs play in all economies regardless of whether they in developed, emergent or developing economies.

References

[5]. OECD (2017): Enhancing the Contributions of SMEs in a Global and Digitalised Economy, Meeting of the OECD Council at Ministerial Level Paris, 7-8 June 2017


