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**THE EFFECTS OF WORKING CAPITAL  
MANAGEMENT ON SME's PROFITABILITY IN  
MALAYSIA**



**MASTER OF SCIENCE (FINANCE)  
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**THE EFFECTS OF WORKING CAPITAL MANAGEMENT ON SME's  
PROFITABILITY IN MALAYSIA**



**BY**  
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Universiti Utara Malaysia

**Thesis Submitted to  
Othman Yeop Abdullah Graduate School of Business,  
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in Partial Fulfillment of the Requirement for the Master of Sciences  
(Finance)**



Othman Yeop Abdullah  
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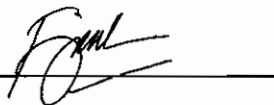
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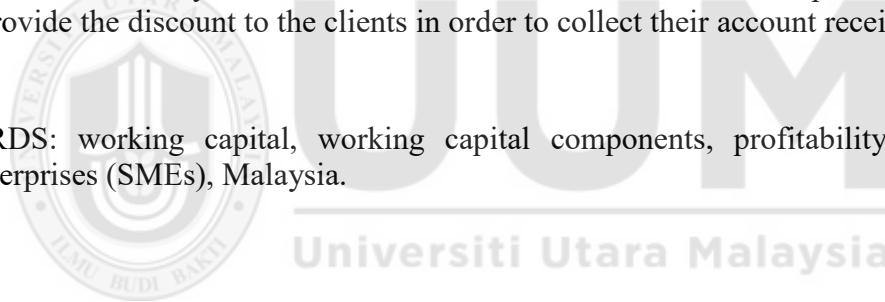
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## ABSTRACT

The inefficient management of working capital not only reduces profitability but in the end may also lead a concern to financial crisis thus every organization regardless of its profit orientation, size and nature of business, needs requisite amount of working capital. Consequently, the efficient working capital management is the most crucial factor in maintaining survival, liquidity, solvency and profitability of the concerned business organization. The objective of this study is to assess the influence of working capital components on the profitability of selected small and medium enterprises (SMEs) in Malaysia. Deductive approach has been incorporated and chose positivism research philosophy. The sample sizes of 58 SMEs have been selected for gathering the financial information in the study. The Statistical Package for Social Sciences (SPSS) has been applied in the study. The relevant data has been gathered for the time frame of five years i.e. 2010 to 2014. Result shows that it is a significant relationship between the working capital management and profitability of the selected firms. Thus, these findings have been suggested to the small and medium enterprises to minimize its borrowings in order to reduce the risk in the company. Moreover, the small and medium enterprises are recommended that they should improve their receivable cycle to ensure that cash is recovered from the parties. Therefore, firms can provide the discount to the clients in order to collect their account receivables.

**KEY WORDS:** working capital, working capital components, profitability, small and medium enterprises (SMEs), Malaysia.



## ABSTRAK

Pengurusan modal kerja yang tidak cekap bukan sahaja mengurangkan keuntungan tetapi pada akhirnya juga boleh membawa kebimbangan terhadap krisis kewangan bagi setiap organisasi tanpa mengira orientasi keuntungan, saiz dan jenis perniagaan, jumlah yang diperlukan untuk modal kerja. Oleh itu, pengurusan modal kerja yang cekap adalah faktor yang paling penting dalam mengekalkan ketahanan, kecairan, keupayaan membayar hutang, dan keuntungan organisasi perniagaan yang berkenaan. Objektif kajian ini adalah menilai pengaruh komponen modal kerja terhadap keuntungan perusahaan kecil dan sederhana (PKS) terpilih di Malaysia. Saiz sampel 58 PKS telah dipilih untuk mengumpul maklumat kewangan dalam kajian ini. Statistical Package for Social Sciences (SPSS) telah digunakan dalam kajian ini. Data yang berkaitan telah dikumpulkan untuk tempoh masa lima tahun iaitu dari 2010 to 2014. Hasil kajian menunjukkan bahawa hubungan signifikan antara pengurusan modal kerja dan keuntungan bagi syarikat yang dipilih. Oleh itu, penemuan ini telah dicadangkan kepada PKS supaya mengurangkan pinjaman untuk mengurangkan risiko dalam syarikat itu. Selain itu, PKS adalah dicadangkan bahawa mereka perlu meningkatkan kitaran terima tunai untuk memastikan tunai adalah dikutip daripada pihak-pihak tertentu. Oleh itu, firma boleh menawarkan diskaun kepada pelanggan dalam usaha untuk mengutip akaun belum terima mereka dengan cepat.

**KATA KUNCI:** modal kerja, komponen modal kerja, keuntungan, perusahaan kecil dan sederhana (PKS), Malaysia.

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# CHAPTER ONE

## INTRODUCTION

### 1.1 Background of the Study

The concept of working capital is referred to as a firm financial position which plays a significant role in maximizing the shareholders' wealth when it maximizes the profits. In order to provide more return on its assets and minimal payment for the liabilities of the firm, it should be able to control the short-term assets and liabilities effectively and efficiently by means of the working capital management. Efficiency in working capital management is a need for every firm to sustain a balance between liquidity and profitability. According Duggal & Budden (2012), working capital management involves managing the short-term assets and short-term liabilities by optimizing its net working capital need which from the difference between short-term assets and short-term liabilities.

Short-term or current assets and liabilities are vital components of the net working capital and therefore firms need to be more careful of analysing them as they play a key role towards the profitability, risks, and the values of firms (Afza & Nazir, 2011 and Smith, 1973). Ganesan (2007) conclude that minimizing the requirements of working capital and maximizing the possible revenues may indicate that the working capital is both balanced and optimal. In addition, if the working capital management is efficient, it may also increase the free cash flow of firms, and the growth opportunities of the firms along with the return to shareholders also are equally greater. Hence, the working capital of the firms should be kept at an optimal level and their values should be maximized (Afza & Nazir, 2007). The efficiency of working capital management is probably to generate significant results and disregard to it by any firm can be highly dangerous (Christopher & Kamalavalli, 2009).



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## APPENDICES

The sample list of 58 small and medium enterprises (SMEs) in Malaysia:

1. A.B.Ng Secretarial Services Sdn. Bhd.
2. A.F.F. Sdn. Bhd.
3. A.L. Wong Motor Sdn. Bhd.
4. Aar Teraspadu Sdn. Bhd.
5. Ada Emasjewel Sdn. Bhd.
6. Advance Vertex Motors Sdn. Bhd.
7. Agensi Pekerjaan Global Man Sdn. Bhd.
8. Alam Tenggara Homemakers Sdn. Bhd.
9. Ampweld Marketing Sdn. Bhd.
10. Asr Padu Sdn. Bhd.
11. Autotech Solution (M) Sdn. Bhd.
12. Baley Concept (M) Sdn. Bhd.
13. Ban Hoe Seng Sdn Bhd
14. Ban Lee Heng Motor (Melaka) Sdn. Bhd.
15. Ban Loong Trading Company Sdn Bhd
16. Bayu Kreasi Sdn. Bhd.
17. Binaan Desjaya Sdn. Bhd.
18. Chin Pek Soo Holdings Sdn. Bhd.
19. Dagang Nusantara Sdn. Bhd.
20. Elegant Avenue (M) Sdn. Bhd.
21. F.Y. Sdn. Bhd.
22. Foo Nyit Tse & Brothers Sdn Bhd
23. Galaxy Techniques Sdn. Bhd.
24. Guan Hoe Company Sdn Bhd
25. Hin Ann Co Sendirian Berhad.
26. Hle Engineering Sdn. Bhd.
27. Inshirah Travel & Tours Sdn. Bhd.
28. Kean Tat Hup Kee (Malaysia) Sdn. Bhd.
29. Kechau Moulding Industries Sdn. Bhd.
30. Kejuruteraan S.B.C. (M) Sdn. Berhad

31. Kemasik Industries (M) Sdn. Bhd.
32. King Hup Industries Sdn. Bhd.
33. Lee Boun Tiong Sdn. Bhd.
34. Leong Hin San Sdn Bhd
35. Pembinaan Khalishew Sdn. Bhd.
36. Perniagaan Teratai Sdn. Bhd.
37. Pine & Hill Wood Products Sdn. Bhd.
38. Poh Teik Enterprise Sdn. Bhd.
39. Poliklinik Kinta Sdn. Bhd.
40. Rapat Tenaga Sdn. Bhd.
41. Seng Yew Trading (M) Sdn. Bhd.
42. Shayo (M) Sdn. Bhd.
43. Sin Meng Kee Products Sdn. Bhd.
44. Sin Wah Lee Motors Sdn. Bhd.
45. Sri Changgong (Kota Bharu) Sdn. Bhd.
46. Syarikat Bernas Edar Sdn. Bhd.
47. Syarikat Germuda Perak Sdn. Bhd.
48. Syl Properties Sdn. Bhd.
49. Synn Heng Trading Company Sdn Bhd
50. T.F. Metal Industries Sdn. Bhd.
51. Tenin (M) Sdn. Bhd.
52. The Ipoh Traders Company Sdn Bhd
53. The Jalan Langgar Transport Company Bhd.
54. Tien Tuck Tong Medical Hall Sdn. Bhd.
55. Ultrawin Sdn. Bhd.
56. Unique Progress Sdn. Bhd.
57. Usaha Pammek Sdn. Bhd.
58. Wira Homeland Sdn. Bhd.

## Descriptive Statistics

**Descriptive Statistics (2010 – 2014)**

	N	Minimum	Maximum	Mean	Standard Deviation
ROA	58	.0009	.3607	.0891	.0748
NOP	58	.0061	12.5583	.6327	1.457
ROE	58	1.323	7.8852	.0455	.1786
CCC (days)	58	-74.4100	161.1294	96.5245	81.8809
RCP (days)	58	6.2305	78.8960	54.8119	32.9798
ICP (days)	58	11.3931	148.1172	72.9878	68.0754
PCP (days)	58	5.0411	77.0861	45.7638	37.6126
FS	58	9.9936	18.2479	14.6397	1.4129
FDR	58	.0219	85.8733	1.5789	8.7121
SG	58	.0002	102.3532	.0054	4.7725
Valid N (listwise)	58				

## Pearson Correlation

**Pearson Correlation (2010 – 2014)**

	ROA	NOP	ROE	CCC	RCP	ICP	PCP	FS	FDR	SG
ROA	1									
NOP	.005	1								
ROE	.322	.088**	1							
CCC	-.030	-.014*	-.048	1						
RCP	-.046*	-.186*	-.042	.350*	1					
ICP	-.054	-.142*	-.048	.966*	.196*	1				
PCP	.027**	-.149*	.036	-.087**	.694*	.069**	1			
FS	-.031	.044	.350	.093**	-.105*	.025	-.242*	1		
FDR	-.012	-.039	-.014	-.037	.023	-.035	.031	-.399*	1	
SG	-.017	-.009	-.004	.006	.048	.002	.056	-.248*	.037	1

\*\* . Correlation is significant at the 0.05 level.  
 \* . Correlation is significant at the 0.01 level.

## Multicollinearity Analysis

**Coefficients<sup>a</sup>**

Model		Collinearity Statistics	
		Tolerance	VIF
1	RCP	.908	1.101
	ICP	.721	1.387
	PCP	.461	2.167
	CCC	.519	1.927
	FS	.869	1.150
	FDR	.578	1.731
	SG	.920	1.087

## Regression Analysis

Independent Variables	Model 1 (DV = ROA)	Model 2 (DV = NOP)	Model 3 (DV = ROE)
Constant	.889147	.154389	-.071246
CCC	-2.03E-05 (0.0562)**	.003374 (0.0005)*	-.000163 (0.3652)
RCP	-.000408 (0.0146)**	-.006214 (0.0053)*	-.000351 (0.6337)
ICP	-4.98E-05 (0.3107)	-.002539 (0.0189)**	-.000301 (0.2503)
PCP	.000410 (0.0349)**	-.001316 (0.6008)	.000195 (0.0533)**
FS	-.000105 (0.5439)	.000539 (0.7965)	8.85E-05 (0.7795)
FDR	-2.45E-05 (0.9355)	-.004132 (0.1649)	-.000401 (0.6843)
SG	-.001674 (0.3988)	.044123 (0.3203)	.007959 (0.3251)
R-square	.498824	.515879	.432217
Adjusted R-square	.428659	.448102	.352727
Durbin-Watson	1.493211	1.508236	1.510674
F-value	0.031493**	0.000296*	0.799845

\*. Significant at the 0.01 level. \*\*. Significant at the 0.05 level.

