

**ASSESSMENT OF NON PERFORMING LOAN ON THE
PROFITABILITY OF MICRO FINANCE INSTITUTIONS (IN
CASE OF METEMEMAN IN MICRO FINANCE)**



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DEPARTMENT OF ACCOUNTING AND FINANCE

**A RESEARCH PAPER SUBMITTED IN PARTIAL FULFILMENT
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AND FINANCE**

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Abstract

This study would be conduct on the title of assessment of non-performing loan in micro finance institutions in metemamen micro finance. The general objective of the study is to assess factors that affect the credit management in micro finance institution of metemamen in wolkite branch. The specific objectives of the study are to analyses the assessment of non-performing loan, to assess the technique, used by institution to manage non performing loan.to analysis the main reason a loan become non performing. To assess after credit provision. In this study both primary source of data was used and the researcher would be used open end and close questionnaires and structured interview to collect data from the employee, customers and management body of the institutions and purposive method was used to collect data from employee and management body of metemamen credit and micro finance institution. And also the researcher was used descriptive method of data analyzing. The general objective of the study is to investigate factors that affect the credit management in micro finance institution of metemamen in wolkite branch. Longitudinal design is employed for a data collection and analysis purpose. The sample would be use selected by purposive sampling selection techniques. There are some problems related with collections of credit given to borrowers and any other related with it. Thus metemamen micro finance institutions and government should take a corrective measurement in order to reduce credit risk management in metemamen micro finance institutions.

Acronyms

MFI: Micro finance institutions

FNGOs: financial nongovernmental organization and credit union

NPLs: Non-performing loans

GNP: Average loan rate

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CHAPTER ONE:

INTRODUCTION

1.1. BACK GROUND OF THE STUDY

According to the International Monetary Fund (IMF,2009);a non performing loan is any loan in which interest and principal payment are more than 90 days overdue; or more than 90 days' worth of interest has been refinanced. On the other hand, Basel committee (2001) puts nonperforming loans as loans left none paid for a period of ninety days. But whatever it is there are no global standards to define nonperforming loans at practical level. Various exist in term of classifications system, scope and content of loans. According to chodoy et, al (2002; page 21-54) states that no performing loans refers to those financial assets from which small micro finance institution no longer receive interest and installment payment as scheduled.

It is obvious that an efficient and well-functioning financial sector is essential for the development of any economy, and for the achievement of high and sustainable growth. One of the indicators of financial sectors health is loan qualities. Even though Granting loans have their own financial and nonfinancial contributions on micro finance institutions, the main problem of granting loans is that loan default. The causes for loan default are different and have a multidimensional aspect. Theoretically there are so many reasons as to why loans fail to perform. Some of these include depressed economic conditions, high real interest rate, inflation, lenient terms of credit, lack of credit orientation, and poor monitoring of loans. In general loans become nonperforming when it cannot be recovered within certain stipulated time that is governed by some specific law.

Most scholars decide that there are two sets of factors on NPLs over the time. One group focuses on external events such as the overall macro-economic conditions which are likely to affect the borrower capacity to repay their loans. While the other group focuses on more about the variability of NPLs across micro finance institution, attributes the level of NPLs to bank.

The essential function of microfinance institution system is to act as intermediaries between other MFIs to borrowers. In addition to that micro finance mainly provides loan service to the

investor. Financial Institutions play a critical role in an economy, therefore it is essential to identify problem that affect the institutions. The main factors that affect the position of micro finance in the development of the economy are nonperforming loans. Nonperforming loan may exist when loan cannot be repaid with in specific date. That is why student researcher motivated to assess of nonperforming loans on of micro finance institutions. Beside to that the researcher was motivated to identify the real cease and control techniques of the intuitions on nonperforming loans.

1.2. Statement of the Problem

The success of MFIs largely depends on the effectiveness of their credit management systems because these institutions generate most of their income from interest earned on loans extended to small entrepreneurs. Extension of credit facilities is one Companies, Rural banks, Financial Non-Governmental Organization (FNGOs) and credit Unions. This is usually evidenced by the large proportion that loans constitute in the overall operating assets of these lending institutions. A World Bank policy research working paper on NPLs in Sub-Saharan Africa revealed that NPLs are caused by adverse economic shocks coupled with high cost of capital and low interest margins (focfac2005). Goldstein and Turner (1996) stated “the accumulation of NPLs is generally attributable to a number of factors, including economic downturn, macroeconomic volatility, terms of trade deterioration, high interest rate, excessive reliance on overly high-priced inter-bank borrowings, insider borrowing and moral hazarding loans or lending operations, microfinance institution faces different forms of risks. The first one is financial risk including both liquidity and credit solvency. The second one is operational risk related to fraud operational error and system related to the information problems. The third and the most types of risk are business risk associated to the microfinance industry as a whole in connection with the overall economy of the nations.

In general, the above risk and other related various reasons affect the collectability of loans on microfinance institutions and have more interruption in credit operations. According to different researcher, there are factor of the non-performing loans. Such as; problems of lack customers, skills, and lack of income social problems, Poor management of nonperforming loans, follow up and collection problems, Timely decision making problems in the case of risk and Collateral assessment in their life span.

As per the knowledge of the researcher, there is some research done on the topic of the impact of nonperforming loans on microfinance institution in recent years. Most studies undertaken in the past few years have focused mainly on credit models used by MFI's and their impact on profitability (Migiri, 2002).Some study mainly focused on the factors causing non-performing loan. For instance there is a research study done on assessment of factors causing nonperforming loans (by KassahunFiseha) .on the above study the researcher mainly focused identifying the factor that causing nonperforming loans. That is why; the researcher will very interest to do a research on this topic so that to identify the main factors that affects profitability of the microfinance.

By taking the above and other facts in account, the research study is trying to address the following questions.

1. What are the main reasons loans becoming nonperforming?
2. What is the major assessment of nonperforming loans of MFI?
3. Which techniques are used by MFI to manage nonperforming loans?

1.3. Objective of the study

1.3.1 General objective

The general objective of the study is to assess the assessment of nonperforming loans on microfinance institution (MFI).

1.3.2. Specific objective

In addition to the above general objective, this study also has the following specific objectives.

- To analysis the assessment of nonperforming loans on micro finance institution.
- To assess the techniques used by Institution to manage nonperforming loans.
- To analysis the main reasons a loans becoming nonperforming.
- To assess after credit provision services of the institution

1.4. Significance of the study

The researcher believes that, the result of this study would have the following significance.

- To show those concerned costs associated with nonperforming loans and its impact.
- To give insight how manager use possible recommendation regarding nonperforming loans.
- Those how are interested to conduct comprehensive study regarding the impact of nonperforming loan on microfinance institutions (MFI).
- More over study also have importance to the researcher giving tangible knowledge by deep finding to NPLs, and also by doing this study to get the reward of Bachelor Degree in the profession of accounting and finance.

1.5. Scope of the study

This study concentrates on metemamen micro finance institution in wolkite branch for the past five consecutive years, from 2013 to 2017. Moreover, the researcher wants to assess the assessment of non-performing loan on smalls Ethiopia MFIs. Therefore, the current based on intensive study limits its coverage on the impact of non-performing loan in small MFIs wolkite town by both primary and secondary data review.

1.6. Organization of the study

It should be organization of the study the research paper is going to have 5 chapters'chapter one: an introduction part includes, background of the study, statement of the problems, objectives of the study, significant of the study, scope and limitation of the study Chapter two: is literature review. It includes: Theoretical literature review Empirical literature review and research gap. chapter three is about research methodology it consists Research Design, Data Type and Source, Methods of Collection, population and sample Design, Methods of Data Analysis Chapter four is data analysis and chapter five is about conclusion and recommendation.

CHAPTER TWO

2. LITERATURE REVIEW

2.1 Theoretical review of literature

2.1.1 Definition of Microfinance

Finance refers to the process by which market deals with cash flows. It is the situation that make possible to borrow and lend or save financial intermediaries are institutions that match borrower and lender or savers. Financial intermediaries include micro finance insurance company and MFIs other informal financial services. It is the first necessary to make explicit definition of microfinance and poverty on which this section attempts to investigate relationship. Microfinance refers to the delivery of financial services of such as credit saving insurance etc. to clients who are without access to the service of formal sector financial institutions on sustainable basis, (Joan Parker 2006). Microfinance, those small scale financial services, primarily credit and saving provided to people who farm or fish or herd and who operate small scale enterprise or micro enterprise where goods and services are produced. Microfinance institutions are often defined as in terms of the following characteristics: Promoting performance loan business, building capacity of the poor, expanding performance loans without collaterals, combining credit without saving and. charging market rate of interests.

“Microfinance” refers to as micro financial institutions to the rural and urban poor to provide credit, self-employment and small business, and including saving and technical assistance. Granting loan is a contractual agreement in which a borrower receives something of value now and agrees to repay the lender at same date in the future, generally with interest. The term also refers to the borrowing capacity of an individual or company (<http://www.wisegeek.com>).

Generally, those rural financial institutions have intended to financial service to clients that are usually extended from formal financing small holder farmers. Women’s and the poor they have done this by employing variety of operating models such as, improved saving.

2.1.2 Evolution of Microfinance

Mobilization and flexibility in service delivered, (Daba and Moti 2006). Economists have proposed several theories of joint liability lending that stresses various aspects of its informational enforcement advantages over other forms of lending institutions that rely on joint liability to facilitate lending the poor have a long history and are now a common feature of money developing countries. The economic models of joint liability lending institutions (JLLI) formalize the idea that a well- structured JLLI can deal effectively with the major problems adverse selections, moral hazard, auditing costs and enforcement facing lenders by utilizing the local information and social capital that exist among borrowers. Most joint liability lending institution operates in environments where borrowers do not have physical asset to pledge as collateral group. Lending have a long practical history but much recent stems from microfinance was intended by Dr Mohammed Yenus, financial project research 1976 as a research project to test the of hypothesis of weather provision of small scale financial services to the poor to reduce their poverty or not. From this research result, it was observed that the concept of lending be rationalized for sustainability. This was evaluated and showed good performance in term of sustainability. In 1983 the project was transformed to grandce banks of the government. The bank puts the mechanism of giving microfinance service to the poor people having objectives of attacking poverty and increase economic of growth and development of the country. Setting group of the lending methodology and group formulation criteria was sated. The bank stated to provide financial service to the poor the evidence provided that, the German banks lends to the poor peoples and others, (Daba&Moti2006).Credit term formulated by the microfinance institutions affect the loan performance; the involvement of credit officer and customers in formulating credit terms affect loan performance (Moti, 2012).

2.1.3 Micro Finance in Ethiopia

In pre 1996 financial service formal establishment MFIs, in Ethiopia is recent phenomenon which can be traced backed ten years. There were however other financial service rendered in the 1970s and 1980,s many international donor, governmental organization and the governmental of Ethiopia have supported the expansion of credit service in country ,mainly rural area .They were not financial intermediaries instead ,They were the tool of distributing fund in order to increasing production and productivity , for instance , if we look at the repayment performance

of agricultural and industrial development bank of Ethiopia it varies between 68% and 11% in 1992 and 1993 respectively. Due to this and other similar problems on the financial service of the economy a legal foundation for the establishment of MFIs was laid in 1996 Genet, 2007

Currently, there are 23 micro finance institutions registered and licensed under NBE and reaching 905000 credit and saving products to clients (Getahun, 2007). The industry is noncompetitive and provides uniform credit saving products to clients. Against poverty through provision of credit and related services like saving, advisory services to potential borrowers particularly to people with little or no purchasing power operational manual of metamamen micro finance association. In pre 1996 financial service formal establishment MFIs, in Ethiopia is a recent phenomenon which can be traced back ten years. There were however other financial services rendered in the 1970s and 1980s many international donors, governmental organizations and the government of Ethiopia have supported the expansion of credit services in the country, mainly rural areas. They were not financial intermediaries instead, they were the tool of distributing funds in order to increase production and productivity, for instance, if we look at the repayment performance of agricultural and industrial development bank of Ethiopia it varies between 68% and 11% in 1992 and 1993 respectively. Due to this and other similar problems on the financial service of the economy a legal foundation for the establishment of MFIs was laid in 1996 Getnet, 2007.

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2.1.4 Role of microfinance on poverty reduction

Poverty could be conceived as a situational syndrome consisting of deficiency in food consumption, high mortality and morbidity levels, poor sanitary and housing conditions and low educational level and existence of widespread marginal populations in all aspects of life. Webster's university defines poverty as 'lack of means of providing material needs and comforts.' According to Joan Parker (2000), poverty has always been a concern of microfinance and some microfinance institutions follow the methods that target a very poor as a separate client group. While other microfinance institutions do their work based on non-targeted financial services to their clients. For all those who lack access to formal credit institutions. Financial intermediation is a process which involves surplus units depositing funds with financial institutions who then lend to deficit

units. Matthews and Thompson (2008) identify that financial intermediaries can be distinguished by four criteria: first their main categories of liabilities (deposits) are specified for a fixed sum which is not related to the performance of a portfolio.

2.2 Assessment of non-performing loans of micro finance institutions

2.2.1 Knowledge of Borrowers

Knowledge on record keeping and business may help borrowers to manage their cash flows and make better business decisions, especially for borrowers who a restarting new businesses. Training and education level (Bhatt, 2002) are believed to be affecting the business performing ability of borrowers. However, Bhatt also points out that training for borrowers could prove to be costly for borrowers who need the loans quickly to capture the opportunities.

2.2.2 The Types of Loans

Different kinds of investment give different returns. Some farm produce may give better returns than other produce. Concentration of types of loan may affect the performance of MFIs. Investment in low earning or high-risk farm products and businesses may result in a lower repayment rate. Specifying the kind of investment for borrowers may be limiting the opportunity and result in higher risks. MFIs should be encouraged to lend to non-farm enterprises and non-farm households (Sacay and Randhawa 1995).

2.2.3 Policy and Objectives

Clear policy has to be communicated well among the staff and clients with proper signals. Without clear policy, communicated objectives may not be set clearly or not taken seriously. Unclear objectives on loan collection, for example, may result in low quality of loan portfolios. Without clear objectives of outreach, loan officers may not concentrate on serving the target group (Holt and Ribe, 1991).

2.2.4 Loan Staff

Loan officers in MFIs have to take care of many small loans and with more borrowers to handle, the monitoring and advisory functions of the staff may be affected and may result in higher loan defaults. Kenya's banking sector involves 43 registered and licensed commercial banks providing banking and financial services to customers (CBK, 2013). The commercial Banks had assets

worth 2.7 trillion as at December 2013 (CBK, 2013). Commercial banks in Kenya play an important role in mobilizing financial resources for investment by extending credit to various businesses and investors. Like any other business, success of banking is assessed based on profit and quality of asset it possesses. Lending represents the heart of the banking industry and loans are the dominant assets as they generate the largest share of operating income. Loans however expose the banks to the greatest level of risk. Prudent credit risk assessment and creation of adequate provisions for bad and doubtful debts can cushion the banks risk. However, when the level of non-performing loans (NPLs) is very high, the provisions are not adequate protection.

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2.2.5 The Schedule and the Amount of Loan Installments

Small and frequent payments may make it easier for small borrowers to manage the cash. Many successful MFIs require small regular repayment from borrowers, recognizing that farm households have many and varied sources of income and types of expenditure (Wright, 2000). Terms of loan payment should reflect the borrowers' needs. According to Wright, institutions with short-term loan products and technologies may be more competitive to informal lenders. Branches with a higher ratio of short-term loans may be doing better financially.

2.2.6 Staff Training

Training of MFIs' staff is considered to affect the performance. Loan collection may be affected by the quality of loan officers. Poor screening and insufficient monitoring of loans affect the quality of loans (Yaron, et.al, 1997)

2.2.7 Management Information Systems

Management information systems are essential for accurate data and monitoring of customers' progress (Sacay and Randhawa, 1995). There should be effective management information systems in tracking payments, due loans, and overdue loans in order to systematically monitor loan performance (Yaron, et.al., 1997).

2.2.8 Incentives for Borrowers

Incentives provided for the borrowers to pay back may be a determinant of repayment rate. More access to credit after full repayments may be a major incentive for borrowers. Continuing access to repeat loans have been identified as a critical factor in keeping a low default rate (Wright, 2000). Inadequate incentive for clients to pay back is a factor that affects the quality of loans (Yaron, et.al., 1997). Borrowers need to have a clear signal from the MFIs that loan repayment is serious. Late payment of loans often occurs because borrowers often test the MFIs, knowing that MFIs are non-Profit organizations and the staffs are not responsible for making profits (Norell, 2002).

2.2.9 Incentives for Staff

A staff incentives system affects the performance of micro-finance institutions. Rewards, including monetary incentives and promotion contribute to the efficiency of successful rural financial institutions (Yaron, et al., 1998).

2.2.10 Loan Amount

Larger loans have greater risk exposure, so the variable costs per-dollar is higher (Schreiner, 2001). If lenders don't take extra care, there could be more loan defaults. Greater loan size means less depth of outreach for the borrower, but usually means more profitability for the lender (Schreiner, 2002). According to Schreiner (2002), average balance, a proxy for depth of outreach, is directly proportional to revenue and default risk. Average loan size to GNP, as a proxy of depth of outreach, was found to have a statistically significant inverse relationship with financial self-sufficiency (Woller, 2002). The amount of loans could be a factor causing NPLs, as it directly relates to risk.

Many MFIs have had problems with the repayments of clients whose loans issued exceed their capacity to repay (Wright, 2000). Higher loan size on the average may imply the overestimation of borrowers' repayment capacity. On the other hand, higher loan size could mean that the borrowers have higher capacity to earn and to repay the loans. Loans too large for business needs may result in the use of loans for personal needs and results in the inability to pay from income (Norell, 2002).

2.2.11 Location

Locations of lending institutions affect the transaction costs of the borrowers and lenders (Bhatt, 2002). It is easier for lenders to acquire information and provide assistance to the borrowers and easier for the borrowers to travel to the lenders with shorter or more convenient routes of transportation. In Sharma and Zellers study (1999), trying to achieve “marginal impact of credit services” may be the cause of concentration of branches of credit organizations in the area with better access to transport and communication infrastructure where clients’ income covariance seem to be lower. Branches with poor locations may cause inconvenience in communication resulting in inefficiency in consultant services and services related to loan collection.

2.2.12 Women’s Participation

Women in many developing countries don’t have as many opportunities as men do in finding jobs and credit. Some argue that women’s participation has led to economic empowerment of women and thus higher loan repayment rates on women borrowers (Bhatt, 2002).

2.2.13 Flexibility for Borrowers to Use the Borrowed Money

This may be an important factor that helps borrowers to take the opportunities of earning better income rather than having to go through the loan application process again. Often loans are diverted because there are better opportunities or emergencies. Wright (2000) points out those successful MFIs do not tie their loans to specific types of projects and where there is a strict policy on providing loans for productive uses there would be a mechanism to provide facilities to meet other needs.

2.2.14 Savings

Egiatsu (1992) claims that the traditional “credit first theory” had serious defects of poor loans recovery. According to Egiatsu, the new view, “the deposit first theory” argued that if the loans are externally funded, borrowers know that there is no “real root in their own economic life”. Some financial organizations consider outside money to be “cold money” and fear that the discipline may be reduced among the members (Wright, 2000). In the case of MFIs, self-financing reduces dependence on external resources and improves financial discipline (Khandker, 1998)

The clients established relationship with the bank may contribute to the necessary data bank used in considering loans and may contribute to better credit assessment and loan collection. Clients and the bank can have some knowledge of each other and feel at ease since more is known before the first loans or larger loans are granted. Clients' savings habit is useful information in credit evaluation (Ravicz, 1998; Matin, Hulme and Rutherford, 2002). More savings could imply that the branches have a good relationship with the clients and have more access to clients' information.

2.2.15 Income of Households

Household income may represent the capacity to pay back the loan. Incomes from other jobs or from other family members may be used for loan repayments and increase the capacity of loan payment (Bhatt, 2002). Since a goal of MFIs is usually to help the poor discriminating those with lower household income by using income as a criterion for credit may seem unsuitable. In trying to cut down some bad loans, the credit officers may be more inclined to consider income of the households as a major criterion for loan approval. Income of the borrowers may be a major factor affecting the ability to repay the loans but may not necessarily affect the willingness to pay. Income fluctuation from ill-health, theft, job loss and fluctuation in demand may have caused dropouts from credit programs (Copes take, Bhalotra and Johnson, 2001).

2.2.16 Interest Rates

Interest ceilings and interest rates fixing has been very damaging because interest rates are critical in the mobilization, and allocation of resources (Yaron, et al., 1997). According to Yaron, et all, governments restrictions on interest rates restrict the levels and types of participation by financial intermediaries in rural financial markets because interest rates on directed agricultural credit are usually fixed below market rates. Restricting interest rates discourages savings and may discourage lending to small borrowers. The demand for loans may not be significantly affected by the level of interest rates (Rhyne, 1998), but interest rate setting is related to client selection (Meyer, 2000). More promising projects might be selected at reasonable market rate. Loan collection performance might be better if poor projects are not selected.

Subsidized rates lead to rationing, which tends to favor the wealthy and politically connected and borrowers might not take the loans seriously enough (Muraki, et al., 1997). Borrowers may take

loans less seriously since the rate is lower than the market rate and money may not be used for the best investment available in the market.

2.3 Empirical Review

Analyzing the potential positive effects associated with group dynamics, some studies examine the impact of different levels of peer selection, peer monitoring and peer pressure. Wenner-- (1995) presents a methodology to test whether the selection mechanism has an impact on the repayment performance of 25 Costa Rican credit groups and whether group members use local information for the screening of their peers. His study shows that lending groups use private information to select their peers and that this selection mechanism increases the group repayment performance. On the same issue, the above-mentioned study of Zeller (2008) confirms the positive role of peer selection (internal rules of conducts) on repayment performance. Wydick (2009) uses data from 137 Guatemalan credit groups to show how social cohesion affects group performance in terms of repayment rates, group insurance and moral hazard. He found that peer monitoring in urban groups and peer pressure in rural ones significantly affects group performance.

Vigano (2003), employing a credit scoring model for development banks based on 118 sample borrowers, taking the case of Development Bank of Burkina Faso, found out that customers characteristics, enterprise characteristics and customers activity, profitability and revenue stability, asset value and composition, financial situation, loan use, bank-customer relationship, contractual conditions and credit risk control, quality of information and the customers banking behavior are identified to influence the bank's credit risk. The study revealed that being women, married, aged, proximity to the bank, use of better technology and being flexible to adjust to market changes, proper use of the loan, project diversification, frequency of loan maturity, collateral, personal guarantee and being a pre-existing depositor are negatively related to loan default risk. Loans in kind, long waiting period from application to disbursement and being younger firm, past default, existence of other loan are those positively related to loan default rate. An empirical study made by Ajayi (2002) on factors which influence default in mortgage finance institution with particular reference to the Federal Mortgage Bank of Nigeria using correlation and multiple regression analysis based on 128 samples (62.7% of the population) showed that default has largely been positively influenced by cost of construction, monthly

repayment, loan to value ratio, market value of property, age of borrower and the annual income of borrower. The expected rental income from property, however, had a negative influence on default.

Hunt (2006) examined the credit rationing technology of lenders and the repayment behavior of borrowers at a rural financial institution based on 504 sample observations. Loan rationing equation and loan repayment equations estimated employing to bit model using survey data at Guyana Cooperative Agricultural and Industrial Development Bank revealed that only 33% of the criteria utilized identified credit worthy borrowers implying that the screening technology was not efficient and needed to be repaired. The results also indicated that tightening the loan contract terms by reducing the grace period on loans and rejecting applications which had long processing times enhanced the pool of credit worthy borrowers.

2.4 Research gap

NPL: determine factors vary from time to time depends on the economic policies, political influences and other factors .as it is clearly evidenced many researchers have been conducted and there is inconsistency up on conclusions. This research unique because it is different in time in and methodology.

CHAPTER THREE

RESEARCH METHODOLOGY

INTRODUCTION

This chapter would discuss about the methodology by which the researcher would use to conduct this study. This section would explain the research design and provides details regarding the population, sample and sampling technique, the research instruments would uses in collecting data for the study and the data collection and data analysis methods.

3.1 Research design

The research design provides a framework or plan of action for the research (Zikmund& Griffin 2009). Based on the nature and objective of the study descriptive research design will use to carry out this study with the survey design.

Descriptive research design will be used in the study. Research design Describes data and characteristics about the phenomena as they exist. Descriptive studies generally take data and summarize it in a useable form. According to Mugenda and Mugenda (2003). The method would appropriately enable the researcher to analyze the Objectives tentatively and also the validity and reliability of the results would be increased.

3.2 Source and Method of Data Collection

The study used primary data sources to gather information from the employee in order to realize research objectives. During the collection of Primary data use questioner, collected using structural interview from credit mangers because, to get relevant data and by using questioners from customers and employees. In the questioners, the researcher would use both close- ended and open- ended questions in such a way that they should generate important information on credit management system of metemamen credit and saving institution. Primary source - questionnaires would administer to both clients and staff of the institution.

Were collects from audited financial statements i.e. Balance Sheet and Profit & Loss Statement of each selected microfinances included in the sample and various journals and related other researches. The data are collected from 2013 to 2017 on annual bases.

As the study needs historical financial data, which are audited financial reports, accessing publicly available data is assumed as the suitable method for the accuracy of the data. According to Bryman& Bell, 2007(cited in Thanh& Carl, 2014), using secondary data can save cost and time and it has very high quality.

3.3. The study population and sampling frame

Target population in the study included all macro finance institution in Ethiopia... But, I am going to conduct my research on Metemamen MFIs in Wolkite branch. In metemamen microfinance institution there are around 6 Employees are exist since, their number was small I would not take a sample them rather used all of them. So i used census method. Census method deals with the investigation of entire Population and provides more accurate and exact information as no unit is left out. In research Methods, population was the total aggregation of items from which samples can be drawn the target population in this research was the entire small microfinance institution which exist.

3.4. The Sampling technique and the sample size

The sampling techniques would used in this research are a non-probabilistic sampling and among the non-probabilistic sampling methods, this research used purposive sampling. As stated by Saunders (2009 pp.232), purposive sampling is often used when working with small samples and when we wish to select cases that are particularly informative. Thus the researcher would used purposive sampling by considering the availability of full data for the selected time period

3. 5 Data analysis Techniques

The researcher processed the data through editing, coding and classifying based on their similarities. After this the data were presented through tabular and percentage. Then descriptive analyses were used on the basis of the summered facts.

CHAPTER FOUR

DATA PRESENTATION INTERPRETATION AND ANALYSIS

Under this chapter attempts have been made to present data in a manner that attract the readers attentions and in a ways that can address the issues that are raised in chapter one of the study. This chapter presents and analyses the data collected through the different data collection techniques. “Questionnaire” is used as a primary data collection method to gather the required information. Section 4.1 presents the qualitative statistics on the finding from the financial institution employees along with demographic profile and their response to the study related questions by using questionnaires. .

4.1. Data Analysis

In addition to the fact in the preceding sections a questionnaires has been designed and was gathered to meet the research questions raised in chapter one of the study. For this studies which requires individual’s response about the assessment of non-performing loan of micro finance institution , the researcher used this data source as a primary source and has got in-depth information by using this technique.

4.1.1 Demographic Characteristics of Respondent

In order to meet the research objectives, data were collected from different respondents of metemamen micro finance such as, gender, age, what type of business the operated and educational level, experience of being (their position)and main business activities of respondents of non-performing loan officers and other representative employees. Summarizes the responses on the gender issue of employees and micro finance main business of the respondents.

Table 4.1 sex, age, and educational background of the respondents.

1 composition	Gender	Item	Respondent	
			Frequency	Percentage
	Male		3	50%
	Female		3	50%
	Total		6	100%
2	Age composition			
		18-25	4	67%
		26-36	2	33%
		36-45	0	0%
		Above 45	0	0%
		Total	6	100%
Qualification composition		10 completed	0	0%
		12 completed	1	17%
		Diploma	2	33%
		Degree	3	50%
		Above degree	0	0%
		Total	6	100%
Work experience.				
		2 years	1	17%
		2-5 years	2	33%
		5-10 years	3	50%
		Above 10 years	0	0%
		Total	6	100%

Source: - survey result and own computation, 2019

From the table 4.1 distribution of gender category most of the employees 50% of the respondent are male and 50% of them are female. In addition to this most of the respondents that is 50% are under the bracket of 18-25 years old. This shows that most of the workers are on the productive age brackets that is range of youngster age. It is very important to the organizations. 67% of the respondents have college diploma and 33% of the respondents have the first degree. This show that in most cases they are educated and skilled it leads to productive for the organization. Concerning their profession 33% of the respondents are accounting & finance, 7.7% economics, 30.7% management and remaining, 30.7% cooperatives accounting and banking and finance area of specifications. Their work experiences also 30.8% and 38.5% of the respondents were maximum they have 2 years and between 2 and 5 years working experiences respectively. This shows that most of the employees are less experienced on their profession. This may affects the institution profitableness and productive level.

4.1.2 Analysis of NPLs and loan Credits

The questions were designed to collect information from credit department employees and -loans officers with regard to responses on NPLs and credit practices. Accordingly, data has been collected and the finding were presented here under in the following few pages.

Table 4.1 Employee response about practical guide line

Questions	Responses	No of respondent	Percentage (%)
What type of loan is granted by MMFI?	Short term	1	17%
	Medium term	3	50%
	Long term	2	33%
	Other	---	---
	Total	6	100%

Source: survey result and own computation, 2019

From the table 4.2 17% loan service are short term loan, it may be increase short run profitability of the intuition but it cannot consider long run capital gain of the intuition. And 33% of loan services are long term loans it has some effect like providing of long term loan leads the institutions to bankruptcy. Because it may be uncertain to payback and also from time to time the interest rate and other financial regulation will be changed and so on. The

long term service of the business depend on the ability to earn sufficient revenue from the customer to offset the benefit of the intuitions from its fund what it granted to the its customers. Therefore table 4.2 shows both positive and negative implications of loans provided by the intuitions.

Table 4.2 employee response on MFIs pre-loans management technique

Questions	Responses	No of respondents	Percentage (%)
Do the MMFI consider customer performances before the granted to them?	Yes	4	67%
	No	2	33%
	Total	6	100%

Source: Survey result and own computation, 2019

From the table 4.2 almost the majority (67%) of the respondents show that the institutions evaluate customer’s performance loans. This shows that have the checking mechanism to grant loan to the customers. It means that the company use pre-granting control techniques to decrease the level of nonperforming loans. But the table also shows that there is some problem on the company to measure the customers before granting the loans to the customers. The remaining 33% of the respondents agreed on this.

Table 3.4 Employee Responses on customer repayment

Questions	Responses	No of respondents	Percentages (%)
Does the customer pay at the right time?	Yes	2	33%
	No	4	67%
	Total	6	100%

Source: Survey result and own computation, 2019

From table 4.4, 33% of the respondents believe that the customers of pay at the right time and 67% of the respondents disagree on this point. This shows that there is week loan provision and collection system. It affects the organizations profitableness by given up good investment opportunity that may invested by uncollected fund from customers.

Table 4.4 Employee Responses on the major cause of NPLs in MMFI

Questions	Responses	No of respondents	Percentages (%)
From your experience which of the following are the major cause of NPLs in MMFI?	Lack of customer awareness	3	50%
	Quality of Employee	2	33%
	Absence of motivation	1	17%
	Total	6	100%

Source: Survey result and own computation, 2019

Table 4.5 shows that most of the respondent 50% answer there is lack of customer awareness about loans. Most of the time the customers use the loaned fund on less profitable area even for personal emergency, this leads unable to repay the loans and become nonperforming ones. And 33% the respondent explain the reason of nonperforming loan is quality of employees' control technique which starts from granting the loans until they repay the loan. As per the respondent of the researcher absence of motivation is not the major factor for loan become nonperforming. So the major case of the non-performing loans is Lack of customer awareness and Quality of Employee about granting and control technique of loan.

Table 4.5 Employee Responses on the assessment of NPLs on Performance of MMFI

Questions	Responses	No of respondents	Percentages (%)
Which of the following are the major assessment of NPLs on the performance of MMFI	On productivity (efficiency) of the organization	2	33%
	On profitability of the organization	3	50%
	On stability of the organization	1	17%
	Others	-	-
	Total	6	100%

Source: Survey result and own computation, 2019

From table 4.6 most respondent or 50% are explained their answer the assessment of nonperforming loan is mainly on the profitability of the organization. But 33% of

Respondents explained that nonperforming affect the productivity of the organization. From this and table 4.5 we can conclude that if there is lack of awareness on the customer about loans leads to decrease the profitableness of the intuitions. This means that profitableness of the intuitions has direct relationship to customer awareness. If the intuitions increase the awareness of the customer, they can possible to increase the profitableness of company.

Table 4.6 Employee Responses on evaluation technique to Minimize risk of NPLs

Questions	Responses	No of respondents	Percentages (%)
From your experience what are the best ways to minimize the risk of NPLs?	To evaluate the borrower ability & willingness to repay	3	50%
	To assess accept/reject decision	1	17%
	Others	2	33%
	Total	6	100%

Source: survey result and own computation, 2019

From the table above 50% of the respondents explained that to minimize NPLs the institution essential to evaluate the borrower ability & willingness to repay the loans. And 17% of the respondents also choice it is better to assess the accept/reject decisions. The remaining 33% of the respondents said that strict follow-up and supervision and loan review of the officers is the important ways to minimize the level of risk. This shows that essential to apply the that is character, capacity and capital of the borrower. Because ability means capacity and willingness means character and capital is financial soundness of the borrower.

Table 4.7 Employee Responses on methods of motivation

Questions	Responses	No of respondents	Percentages (%)
What type of method do you use	By telephone calling	3	50%

	By giving notice	2	33%
	By sending message	1	17%
	Other	0	0%
	Total	6	100%

Source: Survey result and own computation, 2019

From the above table most of the respondents 50% agree on the method of calling by telephone and 33% of the respondents say giving notice to the customer and 17% of them said that by send message to them and the remaining of them said it is better to go to their home or work place and tell them to pay their loans to the institutions and also contact personally and contact with them face to repay the loans. But use telephone calling it is very risky because it is costly and some of the customer may be switch off their telephone or change their phone No and increase the probability of nonperforming loans.

Table 4.8Types of loan gathered by MMFI

Questions	Responses	No of respondent	Percentages (%)
What type of loans do MMFI give to the customer?	Group based loan	1	17%
	Individual based loans	2	33%
	Both of them	3	50%
	Total	6	100%

Source: Survey result and own computation, 2019

From the table above 50% of the respondent that is almost all of the respondents said that provided both individual and group based loans. As we can see from table 4.2 MMFI provided short term, medium term, and long term loans. These two tables show that if there is large number of customer in group or individual to take long term loan it is very difficult to the institutions. Because this grouped peoples may be disagree and become dissolved their business and leads additional cost.

Table 4.9 operation system of MMFI on NPLs

Questions	Responses	No of respondent	Percentages (%)
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How to operate the operations of NPLs?	By manual bases	1	17%
	By computer base	2	33%
	Both of them	3	50%
	Total	6	100%

Source: Survey result and own computation, 2019

From the table above we can see that the operation system of is mainly computer base that is 50% of the respondents agree on this point. Computer based operation system may enable the institution to provide sufficient and quality service at appropriate time and place without significant error. The above data show that the institution also uses manual based operation system, around 17% of the respondents agree on this system. Manual base may be difficult to follow up the customer's situation and very difficult to provide efficient and competent service to the customers. It also leads to corruption because it may be lost of documents if there is manual base of operation system. Manual based may decrease the satisfaction of the customer what provide by the motivation of the customer to return back the loan also may affect similarly. Generally Table 4.12 shows that the company use both computer and manual based system. But as shown the response the intuitions neither use computerized nor manual based rather it was in the process to change from annual into fully computerized technique.

Table 4.10 Employee Responses on treatment of collaterals in MMFI

Questions	Responses	No of respondents	Percentages (%)
How to treat collaterals if loan becomes non-performing & to compensate the loss of the organization?	Sell to market by bid price	1	17%
	Simply use the collateral	3	50%
	Simply sell to the market	2	33%
	Total	6	100%

Source: Survey result and own computation, 2019

As we shown on table 4.11, the institutions use the collaterals rather than sale to the market, 50% of the respondents agree on this point. But 17% of the respondent said the institution

sell it to the market at bid price. And remaining respondents are agreed on the intuitions' sell the collateral to the market if the loans become non performing one. From this we conclude that collateral managing system is very difficult. Because the organization use the collateral; it changes cash to fixed asset and leads to shortage of mobilization of money in the market and affect its liquidity.

In addition to the above data presentation, employee give their opinion on the strength and weakness of the institution, such as create business opportunity to many un employed citizen, provide adequate period to loan repayment, locate easily accessible place to the community poor market assessment, poor staff motivation.

- There is consideration of customer performance to provide loans. It is very important habit of the institutions.
- The evaluation of the customer considers. That is character, capacity, and capital collateral and conditions.
- Using pre and post grant control technique to manage the assessment of nonperforming loans
- Using computerized base of operations.

Weakness (short come of MMFI)

- There is lack of customer awareness about the business.
- Low working experience on their professions.
- The telephoning method is very costly and may also switch off the telephone by the customer.
- Inefficient way of treating collaterals.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATION

5.1 conclusions

This study was conducted on the “Assessment of nonperforming loans on the microfinance institution by taking metemamen as a case area. Metemamen micro finance institution is an institution that provides financial services for its clients or members. Financial institution serves as intermediaries by channeling the saving of individuals, businesses and governments in to loans or investments.

Granting loan is the primary function of micro finance institution. When financial institution granting loan to their customer there may probability for the existence of default loan .It Means that nonperforming loans are controversial issue for all micro financial institution. The researcher interested to assess of nonperforming loans on micro finance intuitions. Especially the researcher study was concerned with identify the major cease of nonperforming loan and control technique to manage it. For this research paper, primary data was used. After the data was gathered from different source, it was analyzed using descriptive methods to the indicated result.

The major parts of data analysis and interpretation are presented as follow:-

- Most (17%) of respondent agreed that, metemamen credit and saving loan service are short term loan. But the institution providing all type of loans.
- Majority (33%) of the respondents show that the institutions concenter customers performance before granting the loans.
- 50% respondent of the study also believes that there is problem on customer to repayment of the loan.
- Most of the respondent agreed on the prevalence of low customer awareness about loans.
- Most respondent or 33% are agreed on the assessment of nonperforming loan is on the profitability of the organization.

- The institution use both manual and computerized operation system.
- almost all of the respondents agreed that provided both individual and grouped based loans
- Most of the respondents believe that the institution essential to evaluate the borrower ability & willingness to repay to minimize the risk of nonperforming loans.
- Most of the respondents argue that to minimize NPLs the institution essential to evaluate the borrower ability & willingness to repay the loans.
- The institutions mostly use the collaterals as compensation for uncollected loan.

Based on the above major finding of the study the following conclusions were made;

As the research finding shows us that, the institution providing all type of loans. That is long term, medium term and long term loans. But it may have its own some effect on the institution. Short term loan of the institution may be increase short run profitability of the intuition but it cannot consider long run capital gain of the intuition. But short term loan may decrease the level of nonperforming loan by narrowing loan repayment time. Long term loan may have some effect on the institution like bankruptcy of the institutions by decrease the amount of loan repayment. Mostly if long term loan increase the level of nonperforming loans. The institutions also consider customer performance before providing or granting loans to the customers. But even though there is consideration, there was also lack of customer awareness about the business for what purpose they borrowed. It means that most of the time the customers use the loaned fund on less profitable area even for personal emergency, this leads to the customer unable to repay the loans and become nonperforming one. The major assessment of NPLs on the institution is that, on the profitability of the organization. Beside to that nonperforming loan affects the institutions' productivity and stability of the organization.

Metemamen credit and saving provides both individual and group based loans. But grouped leads disagreement between individuals and become dissolved their business and leads additional cost. The institution use both manual and computerized operation system. Computer based operation system may enable the institution to provide sufficient and quality service at appropriate time and place without significant error. The custom of customers to repay the loan is very weak. It may affect the organizations profitableness by given up good investment

opportunity that may be invested by uncollected fund from customers. Regarding collateral management of has very poor management system. Because their uses the collateral rather than sale it to the market. It may affect mobilization of money in the market and its liquidity by changing the cash of the intuition into fixed asset of the borrower.

5.2 Recommendations

It was believed that, the key to proper credit administration lies on the ability of the management office. The following are some of the suggestion of the researcher. The porpoise of loans departments and concerned parties for the handling of credit and preventing nonperforming loans;

- The MFI must try to diversify its loans types such as Agricultural loans, Commercial and Industrial loans. Since most of the outstanding balance of the short and long term loans. But the institution must be emphasis on short term loans and medium term loans because short term loans are very importance to the institutions.
- The institution should provide training about entrepreneurship and credit awareness and give technical assistance to the customer before granting the loan.
- Once found are disbursed, the bank should design a system where by borrowers are persuaded to repay their loans regularly. The institutions must have to develop strong

Loan collection and follow-up system to collect the dispersed loans before it becomes non-performing after granting the loans.
- The company should use fully computerized based operation system provide sufficient and quality service at appropriate time and place and for company's attractiveness. And It is advisable to the institution to provide incentives techniques for the borrowers to motivate them to repay back the loan what they borrowed
- The institution must develop a strong credit assessment, analysis and follow-up and also credit review program to facilitate the controls of loans of customers. Generally the intuition should strengthen its own pre and post grant control technique to manage the assessment of nonperforming loans.

- The institution has to increase the number of well experienced professionals, especially proposal analyzing professional to protect false or wrong full business activities. This gives strength to the institutions.

- Finally should use fair market of the collaterals as compensation for uncollected loan. Otherwise It may affect mobilization of money in the market and its liquidity by changing the cash of the intuition into fixed asset of the borrower

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APINDIX

WOLKITE UNIVERSITY

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING & FINANCE

Questionnaire filled by employees

This questionnaire is prepared to collect information for the purpose of research on the title of “Assessment of non-performing loans on micro finance institution” for partial fulfillment of BA Degree in Accounting and Finance. The study is only focused on educational purpose and your responses have never any impact on any other entity. The study area is Metemamen macro finance institution (MMFI, in wolkite branch). I would like to thank you for your cooperation in advance. Uses (√) mark in the box.” Don’t write your name”.

SECTION A: Personal Data

1. Sex

Male Female

2. Age

18-25 above 45
26-36
37-45

3. Education status

Certificate First degree
Diploma Master and above

4. About your work experience

Less than 2 year above 5

2-5

5. What is your area of specification?

Accounting & finance Management
Economics other_specify _____

SECTION B: To analysis the assessment of non-performing loans micro finance institution.

1. Terms of loans granted by MMFI

Short term long term

Medium term

2. What are the major causes of non-performing loan (NPL) on the MFIs?

Lack of customer awareness

Inability of the employee's performance

Absence of employee's motivation

3. Which of the following is the major assessment of NPLs on MFIs?

On productivity of the organization

On profitability of the organization

On suitability of the organization

All

SECTION C: To assess the technique used by institution to manage non-performing loan

4. What are the major causes of non-performing loan (NPL) on the MFIs?

- Lack of customer awareness
- Inability of the employee's performance
- Absence of employee's motivation

5. What type of loans do you give to the customer?

- Group based both
- Individual based

6. How the institution does operate the operation of NPLs?

- By manual basis both
- By computer basis

SECTION D: to analysis the main reason a loan be coming non-performing

7. are the basic requirements granted loans to the customers phase
specify _____

8. Does the micro finance institution consider customer performance before the loan granted?

- Yes
- No

9. What type of contribution does the MMFI played to the unemployed (i.e. frictional unemployment)
please _____ try _____ to _____
explain _____

10. How to treat collaterals if loans become non-performing & to compensate the loss of the organization?

- Sell by the market
- Simply use the collaterals as it is
- Simply sell to the market directly

SECTION E: To assess after credit provision service of the institution

11. Which of the following method is use to motivation of creditors is importance or reducing non-performing loans?

- By telephoning by giving notice
- By sending message other method

12. From your experience what are the best ways to minimize risk of NPLs?

- To evaluate borrower's ability & willingness
- To assessing accepts or reject decision

14. Does the customer pay at the right time?

- Yes No