

**DETERMINANTS OF LOAN REPAYMENT PERFORMANCE IN
MICROFINANCE INSTITUTIONS: CASE OF OMO
MICROFINANCE (OMFI) IN EMDIBER BRANCH**

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LIST OF ABBREVIATIONS

ADCSI:	Addis Credit and Saving Institution
AEMFI:	Association of Ethiopian Micro Finance Institutions
AEMFI:	Association of Ethiopian Micro – Finance Institutions
AfDB:	Africa Development Bank
CBE:	Commercial Bank of Ethiopia
CSA:	Central Statistical Authority
EXC:	Ethiopian Commodity Exchange
GDP:	Gross Domestic Production
GTP:	Growth and Transformation Plan
LPF:	Loan performer software
LRP:	Loan Repayment Performance
MCIs:	Microcredit Institutions
MF:	Microfinance
MFDR:	Micro Finance Development Report
MFI:	Micro – Finance Institutions
NGO:	Non – Governmental Organization
OMF:	Omo Microfinance
OMFCSI:	Omo Microfinance credit and saving institution
OMFIs:	Omo Micro Finance Institutions Share Company
SNNPRS:	Southern Nations and Nationalities Peoples’ Regional State

ABSTRACT

This study was conducted with the aim of analyzing and identifying the factors that influence Omo microfinance loan repayment performance of the clients of Omo microfinance institution. In order to achieve this objective, primary data were collected from 277 respondents using stratified sampling (110 defaulters and 167 non-defaulters). The population was divided into Urban and Rural based on settlement area. The primary data has been collected by interviewing 116 urban borrowers and 161 rural borrowers" respondent using a structured questionnaire with the help of trained enumerators. The questionnaire includes both open-ended and closed-ended questions. In addition, secondary data were gathered from the OMFI head office, OMFI branch office, and other related relevant publications. A binary logit model was used to analyze the socio-economic factors that influence loan repayment. Furthermore, a chi-square(X^2) analysis was employed to compare the defaulters and non-defaulters group.

Keywords: *Microfinance, Omo microfinance, chi-square, Loan repayment, Defaulters, Non-defaulters, and Performance.*

CHAPTER ONE

INTRODUCTION

1.1. Background of the Study

In many developing countries, poverty has become severe leaving millions of people out of basic needs for survival (Fikirte, 2011). To relieve financial constraints and alleviate poverty, MFIs provide financial services to the poor (Godquin, 2004; Fikirte, 2011). In addition, the availability of financial services plays an important role in improving the economic and social status of the poor (Fikirte, 2011; Mokhtar et al., 2012). The eradication of poverty continues to be a top political agenda in most developing countries. In the 1970s the biggest developments in microfinance occurred for the poor people. The microfinance uprising has come a long way since Muhammad Yunus first providing financing to the poor in Bangladesh. Microcredit institutions (MCIs) are institutions that provide small loans to low-income people either individually or as a group (Candice, 2000). Under the individual lending methodology, loans are granted directly to individuals or business entities. The effective repayment history of the individual normally determines accessibility to future larger loans. The group lending methodology involves providing loans to individuals within a group. The group members co-guarantee one another for repayment of the loan to the MFIs, and so providing a form of social collateral. In the case of one member defaulting; the whole group is liable for repayment of the outstanding loan balance, otherwise, they lose future access to loans.

Ghatak and Guinnane (1999) review the benefits of group-based lending in a different manner. Firstly, group-based lending techniques mitigate the information irregularity problems of determining the risk of default by borrowers because groups are normally formed by individuals who are likely to know each other. Secondly, the loans are likely to be effectively invested since members of the group tend to monitor each other constantly. Finally, the members provide a form of insurance to each other within the group for repayment of the MFI loan in case of a genuine reason of default. Hence the concept of social capital by implication, the rest of the members cover up the installment repayment for the defaulting member. Microfinance can be a critical element of an effective poverty reduction strategy. Well organized access and efficient provision of saving, credit and insurance facilities, in particular, can enable the poor to smooth their consumption, manage their risks better, build their assets gradually, develop their microenterprise, and enhance their income earning capacity. Thus, microfinance helps to promote economic growth and development (ADB, 2000).

In developing countries, like Ethiopia, the financial resource is important to input for continuous development. Most of the peoples living in the third world are under the poverty line. They need a wide range of financial services for consumption, running their business and building assets. Due to the lack of collateral, poor people in most cases have no credit access from Banks. Microfinance offers financial services such as loans, savings, and micro insurance to the poor people either in individual or in a group basis to those people. The achievement of microfinance activities in Ethiopia is mainly affected by the income of clients, which directly depends on the effectiveness of the small business of borrowers who live in urban areas; also it depends on crop harvest and the high risk due to drought for rural areas . The fluctuations in product prices, which are difficult to predict, also affect the performance of MFI (Wolday, 2000). Current, most of the microfinance institutions suffer from credit risk, which leads to default. Hence, these studies try to address some determinants of loan repayment that affect both borrowers and lender performance.

Omo microfinance institution is one of the largest MFIs, which are operating in SNNPR, It was established in the year 1997 by Southern Nations, Nationalities, and Peoples' Region to reduce poverty by addressing the financial and related needs of the poor?

Currently, OMFI has 15 branches, 165 sub-branches and 3,888 kebele level credit and saving agents to serve the entire population of the region. OMFI strive to take part and play important role in combating poverty and bringing about sustainable economic development in the region (SNNPR) by providing financial services which stimulate and assist individual initiatives through encouraging self-employment both in urban and rural areas.

1.2. Statement of the Problem

Poverty alleviation was one of the key development challenges over the decades in most developing economies. One of the identified key constraints faced by the poor is lack of access to formal credit. Microfinance institutions are established to fill the gap of scarce finance resources by providing funds to the poor and lower income group to alleviating poverty and improve their business activities. Different approaches have been employed in alleviating poverty; one is the provision of credit for targeted poor. Credit is considered to be an essential input to increase productivity (Nawai and Shariff, 2010). Provisions of credit to the poor take advantage of economic opportunities to increase their level of output hence move out of poverty (Shetty, 2008). The primary objective of MFIs was to provide financial services (credit and

saving) to the poor in order to discharge financial constraints and help alleviate poverty. Microfinance institutions offer loans mostly to urban and rural peoples who cannot afford collaterals to get loans from banks. Financial services in Ethiopia are characterized by high urban concentration (Facet, 2013).

To fill this gap microfinance institutions provide credit to the poor, who lack access to formal credit from financial institutions. One indicator of the effectiveness of MFIs was the loan repayment performance of the borrowers (Addisu, 2006). High loan repayment rates benefit both MFIs and borrowers (Godqin, 2004). Most MFIs in Ethiopia are experiencing default problems as can be observed from their declining repayment rates (Abafita, 2003). The poor loan controlling system causes a serious challenge to most microfinance institutions. Microfinance institutions try to maximize their repayment performance. Improving repayment rates helps reduce the dependence of the MFIs on subsidies, which would improve sustainability (Godquin, 2004). Also, it argued that high repayment rates reflect the adequacy of MFIs services to clients needs. High repayment rate helps to obtain the next higher amount of loan (Bond and Rai, 2009). Contrary to this, if there is a low repayment rate, both the borrowers and the MFI are affected. In this case, the borrowers were not able to obtain the next higher loan and the lender will also lose their customer. Default rates are the number of loans not collected on current and past loan maturity period. Studies on loan repayment were not a new research area. In fact, various researches have conducted in loan repayment performance at a different time, but the results of findings are still debatable among different researchers. The findings show there is the inconsistency of result regarding the determinant factor variables. Some variables such as sex, education level, method of lending and loan size have debatable results. For instance; Fikirte K. Reta and Fitsum Tadele Bhatta and Tang (2002) and Solomon and Addisu (2013), found sex has a significant impact on repayment rate, whereas Godquin (2004) and Jemale (2003) oppose this result. Regarding loan size, Zeller and Sharm (1996) found as loan size have a positive impact on Loan Repayment. Whereas, Jemale (2003) found as loan size have a significant and negative influence on Loan Repayment. Found sex has a significant impact on the repayment rate, whereas opposes this result. Regarding loan size, found as loan size has a positive impact on loan repayment. Whether default was random and influenced by erratic behaviors or whether it is influenced by certain factors in specific situations, therefore, needs an empirical investigation so that findings can be used by Microfinance Institutions to manipulate their credit programs for the better.

Therefore, this study was conducted/ aims to fill the above-mentioned gaps by including additional variables on former researchers on determinants of loan repayment identifying and examining determinants of loan repayment in MFIs in Emdiber branch. Besides, as to the researcher's knowledge, it appears that no study has been conducted on microfinance loan repayment performance in Emdiber city Administration on urban and rural borrowers. The researcher selected this area due to; MIFs such as OMFI is facing financial constraints to sustain loan provision to the poor due to problems in loan repayment performance. Thus, this study is conducted to examine the factors that determine the performance of loan repayment of OMFI, in Emdiber branch. Finally, the findings will expect to fill the literature and knowledge gap observed in the area. Besides, the findings of this study will help to visualize the factors affect loan repayment of borrowers and lenders in the study area.

In general the gap shows; inconsistency empirical Findings, Lack of empirical studies specific to the determinants of loan repayment performance of borrowers in the study area of microfinance institution especially in OMFI and considering the facing financial constraints to sustain loan provision to the poor due to increasing in the default rate of the institution.

Finally, the results from findings and recommendations from this study can be used by governments, non-governmental organizations (NGOs), donor agencies, credit unions and banks in policy making processes which in the long run would help to effectively improve repayment rates of microfinance institutions for sustainability and poverty reduction. It is also hoped that the result of the study will contribute significantly to further studies on microfinance and lending methodologies.

1.3. The objective of the Study

1.3.1. The General objective

The main objective of the study is to investigate and analyze the determinants of loan repayment performance of borrowers and to identify the major problems that face OMFI in Emdiber Branch.

1.3.2. The Specific objectives

- To identify the demographic and socio-economic factors that influences the loan repayment performance of OMF borrowers in Emdiber Branch.
- To assess the major problems faced by the borrowers and lenders in the repayment process related to internal and external factors in OMFI's Emdiber Branch.

- To analyze loan collection performance of Omo microfinance borrowers in a rural and urban area.

1.4. Research Questions

The study has the following research questions were developed to solve the problems:

1. What are the major demographic and socio-economic factors that influence the loan repayment rate of the borrowers of Omo Microfinance Institution (OMFI)?
2. What are the major internal and external problems and challenges of faced by the borrowers and lenders in the repayment process in Omo Microfinance Institution (OMFI)?
3. How to analyze loan collection performance of Omo microfinance borrowers in a rural and urban area?

1.5. The hypothesis of the Study

The repayment rate is expected to be influenced by borrowers' specific characteristics, the project-specific characteristics, and other external factors. Factors expected to affect the loan repayment performance of borrowers are identified on the basis of similar studies done before. Variables that are hypothesized to be input determinants of loan repayment performance in this study were specified as follows:

H1: There is a significant Relationship between demographic characteristics and loan repayment performance among Omo microfinance loan beneficiary in Emdiber branch.

H2: There is a significant relationship between institutional characteristics and loan repayment Performance among Omo microfinance loan beneficiary in Emdiber branch.

H3: There is a significant relationship between Socio-economic characteristics and loan repayment Performance among Omo microfinance loan beneficiary in Emdiber branch.

1.6. Significance of the Study

MFIs are important for poverty reduction and creating employment opportunity especially in developing countries like Ethiopia. One of the key factors for profitability and sustainability of MFIs is the presence of good loan repayment rates. There are a number of socio-economic factors that affect loan repayment rates. Analyzing such factors and planning and appropriate solutions are essential to expanding the activities of MFIs in a sustainable manner. This study tries to provide information for a better understanding of the determinants of loan repayment

performance of the OMF in Emdiber branch from both lender and borrowers side. The primary advantage of this study is to establish a knowledge base that enables to makes a sound decision and take corrective action. In addition, the information was useful for policymakers, other lending institutions, and stakeholders.

This study tries to provide:-

- Knowledge for future references by people who have the interest to gain insight about loan repayment performance of an institution.
- Relevant information to decision makers about loan repayment performance of OMF.
- Baseline data to compare against similar studies to be made in the future in the study area.
- A base for Policymakers to develop policies that will enhance loan repayment rates since they were an understanding of the factors that influence repayment rates.

1.7. The scope of the Study

The study was conducted in Emdiber city Administration, Gurage Zone, SNNPR, in Ethiopia. As stated in the objectives, the main aim of the study was to identify important demographic, socio-economic and institutional factors that affect loan repayment performance of borrowers who borrow from formal credit sources namely Omo microfinance institutions. Accordingly, the study was conducted in Emdiber branch.

1.8. Limitation of the Study

The study was concerned with the analysis of the determinants of loan repayment performance of Emdiber branch small-scale farmers and therefore did not consider borrowers from informal credit sources. This limitation is attributable to the time constraint and the relatively higher asymmetry of information in informal circles. Therefore, the study was undertaken to meet its objectives within the above limitations.

There are also many factors affecting the sustainability of MFIs such as outreach, repayment performance, policy support, and using innovative features. But this study covered the repayment aspects of microfinance in the case of Omo MFI and focused on the socioeconomic factors that are associated with repayment.

1.9. Organization of the study

This research paper consists of five chapters. The first chapter compresses background of the study, statement of the problem, objectives of the study, significance of the study, scope of the study and Organization of the study. Chapter two presents literature review with respect to the theoretical perspective and empirical studies on microfinance. Chapter three provides the research design and method of data collection of the study, in addition includes the main principles of research methodology and the adopted research design for the study. Chapter four consists of presentation of data, analysis of findings, and interpretation of the collected data on the problem in the sample.

Finally, chapter five consists of summaries of major findings, conclusions, and recommendation for possible solutions to the problems of the study.

CHAPTER TWO

2. LITERATURE REVIEW

2.1. Theoretical Review

2.1.1. Overview of Micro Finance

Microfinance refers to the provision of financial services to low-income clients, including consumers and the self-employed (Ledgerwood, 2000). The word microfinance refers to small-scale financial services primary credit and savings provided to people who operate small enterprises, provide services, fish farm or herd, and to other individuals or groups at local level of developing countries both rural and urban areas (Robinson, 2001). Canadian International Development Agency (CIDA, 2007) defined microfinance as, “the provision of a wide range of financial services to poor women and men to enable them to increase their incomes, build assets and reduce lack of access to formal financial institutions. microcredit, which is likely the most visible form of microfinance, but also saving, micro insurance, money transfer, and other financial services.

2.1.2. Microcredit and Microfinance Definition

The Grameen Bank defined microcredit as small loans given to the poor for undertaking self-employment projects that would generate income and enable them to provide for themselves and their families. The target populations comprising women microenterprises from low-income households and the loans have no collateral. However, microfinance is defined as the provision of financial services to low-income clients, including consumers and the self-employed, who traditionally lack access to banking and related services (Gonzalez-Vega, 2008). Microfinance is a place for the poor and near-poor clients to get access to a high-quality financial service, which includes not just credit but also savings, insurance, and fund transfer. According to Ledgerwood (1999), microfinance is a provision of a broad range of financial services such as savings, credit, insurance and payment services to the poor or low-income group who are excluded from the normal banking sectors.

Microfinance is a development approach that provides financial as well as social intermediation. The financial intermediation includes the provision of savings, credit and insurance services, while social intermediation involves organizing citizens’ groups to voice their aspirations and raise concerns for consideration by policymakers and develop their self-confidence (Robinson, 2002). The World Bank defines microfinance as “Small-scale financial services primarily credit

and savings provided to people who farm or fish and who operate small enterprises or microenterprises where goods are produced, recycled, repaired, or sold; who provide services; who work for wages or commissions; who gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban” (Robinson, 2001).

Therefore, based on all definitions given, it can be concluded that microcredit is just a small credit given to the poor that engaged in microenterprise or for the purpose of income-generating activities. On the other hand, microfinance encompasses broad financial services given to the poor and low-income group for many reasons and not just for income generating activities.

Woller & Parsons (2002) describe microfinance as the second revolution in credit theory and policy where the first revolution is microcredit. Microfinance institutions (MFIs) were established to fill the gap in the financial services sector by providing funds to the poor and lower income group and thus alleviating poverty and enhance their business activities. The MFIs provide funds for a start-up business or for working capital. In addition, some MFIs also provide funds for non-business activities such as for education and emergencies purpose. In the credit market, agency problem, moral hazard and adverse selection exist because of information asymmetries. Information asymmetries are the main obstacle for MFIs to provide loans to clients. Financial institutions usually require a business proposal, borrower past credit information and collateral before approving the loan. MFIs offer credit through the group-based lending method to mitigate agency problems, moral hazard, and adverse selection and to replace the collateral requirement. In group-based lending, borrowers must form a group before applying for loans and they also respond to other loan members. If one member default, the others will be responsible to pay the loan or they will be denied access for the next loans.

2.1.3. Characteristics of Microfinance

Microfinance gives access to financial services to low-income people, who wish to access money for starting or raising an income generation activity. The individual loans and savings of the poor clients are small. Microfinance came into being from the appreciation that micro-entrepreneurs and some poorer clients cannot have access to borrow from banks, that is, they can repay, both the principal and interest, on time and also make savings, provided financial services are tailored to suit their needs. Microfinance as an institution has created financial products and services that together have enabled low-income people to become clients of a banking intermediary.

The characteristics of microfinance products include (Murray and Boros, 2002, pp.10-11).

- Small amounts of loans and savings.
- Short- period loans (up to one year term).
- Payment schedules attribute frequent installments or frequent deposits.
- Payments (Installments) made up from both principal and interest.
- Higher interest rates on credit (higher than commercial bank rates)
- Easy access to the microfinance intermediary saves the time and money of the client and permits the intermediary to have a better idea about the clients' financial and social status. simple application procedures
- Short processing periods (between the completion of the application and the disbursement of the loan)
- The clients who pay on time become eligible for repeat loans with higher amounts.
- No collateral is required contrary to formal banking practices. Instead of collateral, microfinance intermediaries use alternative methods, like, the assessments of clients' repayment potential by running cash flow analyses, which is based on the stream of cash flows, generated by the activities for which loans are taken.

2.1.4. Challenges of microfinance

Microcredit (MC) as a tool of poverty alleviation and it faces various challenges. These can be understood at three different levels: macro, meso, and micro. At the macro level, unstable policies and poor macroeconomic conditions (economic growth and stability) are crucial to MC development. At meso level, the inadequacy of institutional capacities those are; managerial and financial worthiness, quality of the human resource, lack of coordination among the MCIs, entrepreneurial skills, and the issue of sustainability (mainly financial) are the main limitations. At the micro level, the Problems related to the creditworthiness and credit discipline of the clients are the main challenges (Samuel, 2008, p.23). According to Vento (2004), the first most typical challenges faced by any Microfinance institution is a credit risk. In addition, the cost of debt collection per loan amount is, on average, higher than in formal intermediation, especially in developing countries lending.

The first most typical challenges faced by any Microfinance institution is credit risk as mentioned earlier. Moreover, the cost of debt collection per loan amount is, on average, higher than in formal intermediation, especially in developing countries lending (Vento 2004).

Similarly, the high cost of service associated with the low-value, high volume and cash-intensive nature of the business and also high fixed and variable costs (Basu, 2005).

The second source of risk for MFIs is represented by interest rate risk; it can be significant in the case of MFIs that collect deposits too. In most developing countries, the average higher interest rate is volatile. Similar to interest rate risk, liquidity risk also appears more significant for deposit-taking MFIs; in fact, small savers tend to make frequent withdrawals and deposits, therefore, managing liquidity could become more difficult (Vento 2004). Moreover, Basu (2005) stated that risk management challenges are associated with high levels of information asymmetry.

Another source of challenges in MFIs is ownership and governance risk. This risk concerns the weakness in internal control systems, which play an important role especially in case of lack of external regulation (Vento 2004). In addition, limited management capacity in MFIs and institutional inefficiencies also challenges (Campion, 2002). Moreover, the inadequacy of well-trained personnel in their roles and staff incentives within any formal organization paradigm (private or public) that seeks to deliver these services is challenging for Microfinance institutions (Basu, 2005).

2.1.5. The Concepts of Loan Delinquency and Loan Default

Several researchers have given several but touching definitions of loan delinquency and default. CGAP (1999) describes a loan as delinquent when a payment is late. A delinquent loan becomes a defaulted loan when the chance of recovery becomes minimal (Addae-Korankye, 2014). In the view of Ameyaw Amankwah (2011), default occurs when a debtor has not met his or her legal obligations according to the debt contract. According to Murray (2011), a loan default occurs when the borrower does not make required payments or in some other way does not comply with the terms of a loan. Balogun and Alimi (1990) also define loan default as the inability of a borrower to fulfill his or her loan obligation as at when he or she falls due.

A loan is delinquent when a payment is late (CGAP, 1999). A delinquent loan becomes a defaulted loan when the chance of recovery becomes minimal. Delinquency is measured because it indicates an increased risk of loss, warnings of operational problems, and may help to predict how much of the portfolio will eventually be lost because it never gets repaid.

There are three broad types of delinquency indicators: collection rates which measures amounts actually paid against amounts that have fallen due; arrears rates measures overdue amounts

against total loan amounts; and portfolio at risk rates which measures the outstanding balance of loans that are not being paid on time against the outstanding balance of total loans (CGAP, 1999). Default occurs when a debtor has not met his or her legal obligations according to the debt contract. For example, a debtor has not made a scheduled payment or has violated a loan covenant (condition) of the debt contract (Ameyaw-Amankwah, 2011). Default is the failure to pay back a loan. The default may occur if the debtor is either unwilling or unable to pay their debt. A loan default occurs when the borrower does not make required payments or in some other way does not comply with the terms of a loan. (Murray, 2011). Moreover, Pearson and Greeff (2006) defined default as a risk threshold that describes the point in the borrower's repayment history where he or she missed at least three installments within a 24 month period. This represents a point in time and indicator of behavior, wherein there is a demonstrable increase in the risk that the borrower eventually will truly default, by ceasing all repayments. The definition is consistent with international standards and was necessary because consistent analysis required a common definition. This definition does not mean that the borrower had entirely stopped paying the loan and therefore been referred to collection or legal processes, or from an accounting perspective that the loan had been classified as bad or doubtful, or actually written-off. Loan default can be defined as the inability of a borrower to fulfill his or her loan obligation as at when due (Balogun and Alimi, 1990).

2.1.6. Causes of Loan Delinquency/Default

According to Ahmad, (1997), causes of loan default include; lack of willingness to pay loans coupled with the diversion of funds by borrowers, willful negligence and improper appraisal by credit officers. In addition, Hurt and Fesolvalyi (1998), cited by Kwakwa, (2009) found that, corporate loan default increases as real gross domestic product decline, and that the exchange rate depreciation directly affects the repayment ability of borrowers. Balogun and Alimi (1988) also identified the major causes of loan default as loan shortages, delay in the time of loan delivery, small farm size, high-interest rate, age of farmers, poor supervision, non-profitability of farm enterprises and undue government intervention with the operations of government-sponsored credit programs. Moreover, Akinwumi and Ajayi (1990) found out that farm size, family size, the scale of operation, family living expenses and exposure to sound management techniques were some of the factors that can influence the repayment capacity of farmers. According to Olomola (1999), loan disbursement lag and high-interest rate can significantly increase borrowing transaction cost and can also adversely affect repayment performance.

2.1.7. Lending Methodology

Lending to the poor or lower income group raises many debates among practitioners and academicians. The poor are usually excluded from credit facilities because of many reasons. These include insufficient collateral to support their loans, high transaction costs, unstable income, lower literacy, and high monitoring costs. Usually, they survive through involvement in micro-business activities or informal activities that comprise food processing and sales, small scale agriculture, services, crafts, and petty trading. However, these activities actually contribute a number of total employment and gross domestic product (GDP) to the country. Micro and small enterprises (MEs) have been recognized as a major source of employment and income in many countries of the Third World (Mead & Liedholm, 1998). Lending methodologies differ with respect to whether loans are made to groups or to individuals. The lending methodology selection greatly influences product design, client selection, the application as well as an approval process, loan repayment, and monitoring and portfolio management. The lending methodology also impacts the institutional structure and staff requirements, including training and compensation (Ledger wood, 2013).

2.1.7.1.Individual-based lending

Individual lending requires greater honest analysis of clients and their cash flows, sometimes physical collateral, and frequent and close contact with clients during the term of the loan. Loan approvals and amounts are based on an applicant's eligibility and debt capacity, which in turn are dependent upon a number of factors, including personal and business characteristics, for example, age, gender, or reputation, sources and amount of income, age of business, cash flow, and available collateral (Ledger wood, 2013).

2.1.7.2.Group-based lending

Since the 1970s, group lending programs have been promoted in many developing countries (Zeller, 1996). The key feature of group lending is a joint liability. This means all group members are treated as being in default if any one member of the group does not repay his/her loan. Therefore, each member is made responsible for the repayment of loans of his or her peers (Besley and Coate 1995). Most schemes give subsequent credit only if the group has fully repaid its previous loan. Loan under joint liability shows the threat of losing access to future credit incites members to perform various functions, including screening of loan applicants, monitoring the individual borrower's efforts, and enforcing repayment of their peers loans (Zeller,

1996). When performance is measured with a repayment rate, group lending shows a mixed success (Huppi and Feder 1990). Moreover, Besley and Coate (1995) point out that group lending has both a positive and negative effect on repayment rates. The existing theoretical models of peer monitoring assumes that the repayment performance in the group-lending program is positively related to the homogeneity of group members with respect to the riskiness of their projects (Stiglitz 1990; Devereux and Fische 1993; Besley and Coate 1995) cited by (Zeller, 1998). Zeller (1996) discusses that since the risk of loan default by an individual is shared by his or her peers, a member may choose a riskier project compared to that in the case of individual contract, and may count on other members to repay his or her loan (i.e. adverse selection of risky projects). He further notes that repayment incentives for a good borrower will disappear under joint liability when he or she expects that a significant number of peers will default. Group-based lending is one of the new approaches to lending small amounts of money to a large number of clients who cannot offer collateral. The size of the group can vary, but most of the time groups have between 4 to 8 members. The group self-selects its members before acquiring a loan. Most MFIs require a percentage of the loan that is supposed to be saved in advance, which points out the ability to make regular payments and serve as collateral (Murray and Boros, 2002). According to (Murray and Boros, 2002) group members are jointly accountable for the repayment of each other's loans. To ensure repayment, peer pressure and joint liability work very well. The defaulter group will be disqualified and will not be eligible for further loans, even if one member of the group becomes a defaulter. The creditworthiness of the borrower is therefore determined by the members rather than by the MFI. According to Nawai and Shariff (2010) in group-based lending, borrowers must form a group before applying for loans and they also respond to other loan members. If one member default, the others will be responsible to pay the loan or they will be denied access for the next loans.

2.1.8. Microfinance in Ethiopia

Microfinance institutions introduced in Ethiopia after the downfall of the Derg regime following the policy of economic liberalization. The development of microfinance institutions in Ethiopia is a recent phenomenon. Ethiopian development strategy is the establishment of sustainable microfinance institutions serving a large number of poor people. Microfinance is taken as a shift from government and NGO subsidized loan programs to finance services run by specialized financial institutions. Later microcredit programs were changed to microfinance institutions. Non-governmental organization (NGO) credit schemes and informal sources of finance have existed in Ethiopia for many years; the government instituted a legal and policy framework for

MFIs in 1996 through Proclamation 40/1996 (Gebrehiwot, 2002). Currently, the Ethiopian microfinance industry is rapidly growing. Recently, there are 31 MFIs reaching around 2.4 million people (AfDB, 2012). The deposit interest rate is 3-8% and lending interest rate is 12-24% in 2012. Most MFIs are doing remarkably well in terms of financial performance given their relatively short track record (Facet, 2013).

2.1.9. Omo microfinance institution (OMFI)

After the introduction of proclamations 40/1996, one of the MFI established in Ethiopia is Omo Micro Finance Institution S. C (OMFI) which is operating in the southern nation's nationality and peoples the Regional State of Ethiopia. It was originally established as Nongovernmental organization in 1997. OMFI is operating in nine (9) branches in the following towns of the Southern Nations and Nationalities Peoples Regional State (SNNPRS) such as, Wolkite (Gurage Zone); Hosanna (Hadiya Zone); Durame (Kembata, Alaba Tembaro Zone); Arbaminch (Gamogofa Zone); Bonga (Kaffa and Sheka Zone); Awassa (Sidama Zone); Dilla (Gedio Zone); Mizan (Bench Maji Zone) and Sodo (Wolayita Zone). Total Number of Woredas Covered so far is 52 Woredas in 9 branches. It provides financial services to active poor peoples in southern regional states both in urban and rural areas. Currently, the institution has more than 327,888 active borrowers and gross loan portfolio of USD 31.2 million. The institution reaches its target through the organizational structure, namely: head office, branch office, sub-branch office and kebeles service delivery post. The total number of employees in the institution is 214, out of which 66 are loan officers and the rest are support staffs (OMFI, 2013).

Concerning loan size and loan terms, OMFI provides loan to a micro business, agricultural, small investment and working capital to its diverse clientele. Accordingly loan size for agriculture and micro business loan ranges between 2000 up to 5000 birrs with a loan term of between three months and two years depending on the type of activities financed. On the other hand, Loan size for a small investment and working capital, start with a minimum of birr 5000 depending on the viability, profitability and absorption capacity of the client's enterprise, with loan term extended from a minimum of two years up to 5 years depending on nature the business being financed. In addition to this, the first loan cycle size shall not exceed birr 1,000 and birr10, 000 for agricultural and business loans and small investment and working capital respectively (OMFIOPM, 2010).

2.1.10. Client Selection Criteria and Basic Requirements

Some of the selection criteria for credit service are:-economically active, healthy and capable poor between age group 18 and 60years, low income urban, low-income civil servant, good and proven credit history, willing to make compulsory saving and viability of business plan are the main criteria. In addition to this group formation is one of the key element in MFI, the group will consist of a maximum of 5 members and a minimum of 3 (OMFI, 2010).

A. The obligation for loan clients

OMFCSI is providing loan for borrowers only who fulfill the following criteria:

- Borrowers above the age of 18 years,
- Residence of Emdiber city Administration, either engaged or ready to engage in the micro and small scale business, has a permanent working place,
- Graduates of technical and vocational training (TEVT) in an organized form of cooperatives or business group, certificate for business activities requiring loan size exceeding 5000 birr's,
- The business should be implemented in the Emdiber city Administration and loan are taken from the institution or similar institution should be settled beforehand (OMFCSI, 2019).

The main client screening mechanisms of the institutions are business profitability and experience, the interest in doing business, and client's behavior. In order to know the behavior of clients especially for group lending, they were collected historical background from different stockholders such as Women, & Youth associations and small scale enterprise. In addition, they checked the amount of money requested by the client is enough for doing business or not; they have to control under and over finance. OMFI has been implemented different kinds of loan guarantee and property collateral mechanisms for the loan. The most commonly used are group guarantee (joint liability), the salary of permanent employees of a different organization, collateral (a house or vehicle), clients of the institution based on their savings or business enterprise can be used as a guarantee (OMFI, 2018).

B. Basic Requirements for Credit Decisions

The OMFI has uniform basic requirements which applicants are expected to present and become eligible for a loan. Thus, credit decisions of the microfinance are based on the fulfillment of these requirements as mentioned below.

- Way of land owned
- leased and own plan
- The borrower marriage certificate if engaged in marriage
- Proof of taxpayer
- I.d. Card of kebele, its photocopy

To be qualified for credit, every applicant should fulfill the previously mentioned requirements. If the borrowers full fill the requirements set by the microfinance on the checklist, the client will be eligible for the loan. In the lending process, the microfinance prefers the business plane type and applicant creditworthiness as a first way out and collateral is the second way out as the basis for lending.

However, the microfinance prefers the collateral base of lending because of the following main reasons:

- The economic level of the country: the living standard of society, poverty, etc.
- The culture of the society in lending is at its infant stage.
- The educational level of the society.
- Limited resources of the microfinance (this is to minimize the shortage of finance).
- It is believed to be a harmless way of lending in minimizing credit risk.

C. Amount of Loan Disbursed and Loan Defaulted

Based on the introductory data collected, the OMFI default rate of last five years on the average reach around 31% selected borrowers in the agriculture, commercial, enterprise, and service sector. In view of that, the past five years (2008 E.C-2012 E.C) summary of group, individual and cooperative borrowers loan repayment performance (default rate) at Emdiber branch Omo microfinance institution is presented in Table 2.2 below.

Table 2.1: Performance of Emdiber OMFI Branch during Hamle 2008 E.C-2012 E.C.

Year	Hamle 2008	Hamle 2009	Hamle 2010	Hamle 2011	Hamle 2012
Disbursed Loan	22,084,104	24,128,708	18,870,880	19,722,944	43,772,202
Loan Collected	14,413,210	17,537,699	14,824, 963	15,092,093	22,375,719
Loan Defaulted	7,670,894	6,591,009	4,045,917	4,630,851	21,396,483
Default rate	35%	27%	21%	23%	49%

Sources: Field result OMFI (2013 E.C)

2.2. Factors Affecting Repayment Performance

2.2.1. Individual/ Borrower Characteristics Affecting Repayment Performance

Some authors link the repayment performance with firm characteristics such as Nannyonga (2000), Arene (1992) and Oke et al. (2007) (Table ii). Oke et al. (2007) mention that the firm's profit significantly influenced loan repayment. Besides that, Khandker et al., (1995) raise the question of whether the default is random, influenced by erratic behavior, or systematically influenced by area characteristics that determine local productions conditions or branch-level efficiency. Their study on Grameen overdue loans supports the idea of the partial influence of area characteristics. Rural electrification, road width, primary educational infrastructure, and commercial bank density are positively correlated with a low default rate as well as predicted manager's pay.

2.2.2. Firm Characteristics Affecting Repayment Performance

Godquin (2004) suggests that the provision of non-financial services such as training, basic literacy and health services has a positive impact on repayment performance. Roslan & Mohd Zaini (2009) found that borrowers that did not have any training in relation to their business have a higher probability of default. Tedeschi (2006) notes that there are two possible reasons for default: strategic default or default due to a negative economic shock. The lending contract provides incentives to discourage strategic default, but default due to an economic shock is unavoidable. In contrast, Hulme & Mosley (1996) argue that the important factors contribute to loan repayment performance are the design features of the loan. They categorize the design features into three categories namely access methods, screening methods and incentive to repay. Access methods generally ensure that poor people access the loans not the richer people and the features include maximum loan ceilings and high-interest rate. Screening methods are used to screen out bad borrowers. However, Stearns (1995) argues that "it is the lender, not the borrower, who causes or prevents high levels of delinquency in credit programs. While, Awoke

(2004), reports that most of the default arose from poor management procedures, loan diversion, and unwillingness to repay loans. Therefore, the lenders must devise various institutional mechanisms that aimed to reduce the risk of loan default.

2.2.3. Institutional/Lender Characteristics Influencing Repayment Performance

A few researchers also found that loan characteristics play an important role in determining repayment performance (Roslan & Mohd Zaini, 2009; Njoku, 1997; Ugbomeh et al., 2008) Copisarow (2000) found that defaults generally arise from poor program design or implementation, not from any essential problems with the borrowers.

2.2.4. Loan Characteristics Affecting Repayment Performance

According to Derban et al. (2005), the causes of non-repayment could be grouped into three main areas: the inherent characteristics of borrowers and their businesses that make it unlikely that the loan would be repaid. Second, are the characteristics of lending institution and suitability of the loan product to the borrower, which make it unlikely that the loan would be repaid? Third, is a systematic risk from the external factors such as the economic, political and business environment in which the borrower operates? Vigenina & Kritikos (2004) find that individual lending has three elements namely the demand for non-conventional collateral, a screening procedure with combines new with traditional elements and dynamic incentives in combination with the termination threat in case of default, which ensure high repayment rates up to 100 percent.

Roslan Abdul Hakim et al. (2007) in their study concluded that close and informal relationship between MFIs and borrowers may help in monitoring and early detection of problems that may arise in non-repayment of loans. In addition, cooperation and coordination among various agencies that provide additional support to borrowers may help them succeed in their business. The study compared the good practices and performance of selected MFIs in Malaysia namely; Amanah Ikhtiar Malaysia, TEKUN, Koperasi Kredit Rakyat and Bank Pertanian Malaysia. However, Addisu (2006) categorized repayment problems into four factors: (a) borrower related cause, (b) business operation related cause, (c) lender related to cause and, (d) extraneous causes.

2.3. Empirical Studies on Determinants of Loan Repayment performance

Loan repayment performance is affected by a number of socio-economic and institutional factors. While some of the factors positively influence the loan repayment, the other factors are negatively affecting the repayment rate. Regarding the loan repayment performance of

borrowers, several studies have been conducted in many countries by different authors. Some of the studies are summarized below.

2.3.1. Empirical Studies in Ethiopia and other countries

A study undertaken by Bassem (2008), on main factors vulnerable to affect the repayment performance of group lending in Tunisia reveal that the repayment is influenced positively by the internal rule of conduct, the same business, the knowledge of the other members of the group before his formation, the peer pressure, the self-selection, the sex, the education, and the non-financial services and tie with the loan officer. However, the homogeneity and the marital status are among the main factors acting negatively on the repayment performance of credit groups. A study on group size and social ties in microfinance institutions conducted by Abbink, Irlenbusch, and Renner (2006) indicated that microfinance programs provided poor people with small loans given to jointly liable self-selected groups. Follow-up loans provided incentives to repay. In this study, they experimentally investigated the influence of those features on strategic defaults. Each group member invested in an individual risky project, whose outcome was known only to the individual investors. Subjects decide whether to contribute to group repayment or not. Only those with successful projects could contribute. The experiment ended if too few repay. This investigated group size and social ties effected and observed robust high repayment rates. A study conducted by Wenner (1995) on group credit as a means to improve information transfer and loan repayment performance in Costa Rica found that members of groups engaged in formal screening with an internal code of regulations had a low probability for delinquency, indicating that screening indeed resulted in an informational efficiency gain, a result which is supported by Zeller (1998).

A study on key factors of joint-liability loan contracts by Alexander and Denitsa (2004) reported that joint liability induces a group formation of low-risk borrowers. Furthermore, the incentive system leads to peer-measures between the borrowers, helping the lender to address the moral hazard and enforcement problem. They also demonstrate that the mechanism realizes high repayment rates if the loan officers fulfill their complementary duties in the screening and enforcement process.

Another study was conducted by Onyeagocha, Chidebelu, Okorji, Ada-Henri, Osuji, and Korie (2012) on an examination of determinants of loan repayment of microfinance institutions in southeast states of Nigeria reveal that out of nine explanatory variables, five variables were found to be significant for the probability of being defaulter; that is group size, shocks, training

duration, loan size, and credit officers experience were significantly influencing loan repayment performance of MFIs. However, the remaining four explanatory variables namely, gender, age, interest rate, and methodology had no significant effect on the loan repayment performance.

Roslan and Mohd (2009) undertook a study on the determinants of loan repayment among microcredit borrowers in Malaysia by dividing determinants into three categories - characteristics of borrowers, characteristics of the project or business and the characteristics of the loan. Their result indicated that the probability for loan repayment default was influenced by the gender of the borrower, type of business activity, amount of loan, repayment period and training.

Determinants of repayment performance of credit groups in Madagascar were analyzed by Zeller (1996). He found that groups with a higher level of social cohesion have a better repayment rate. Moreover, the programs that provide saving service to their members have a significantly higher repayment rate.

An investigation of the key factors that influence loan repayment performance among group clients of microcredit institutions (MFIs) in Tanzania has been carried out by Francis and Abel (2009). According to their findings, experience, training time, and sanctions have positive and significant effects on loan repayment performance among group clients of MFIs. However, transaction costs and group size have negative and significant effects on loan repayment performance. An investigation by Alessandra, Luke, and Bruce (2005) on the effect of social capital on group loan repayment found a direct relationship between default and homogeneity, which is the increment in the homogeneity of the group members, would lead to the higher repayment.

As per empirical analysis on determinants of repayment performance in credit groups by Zeller (1998) implementation of internal rules and regulations by the group members would lead to the better repayment performance that is a decrement in the cost of operations of the lender and decrement in the default rate. To sum up, as mentioned above, various studies were conducted in various countries (outside Ethiopia) on the determinants of group loan repayment performance. Most of these studies have identified major factors influencing group loan repayment performance and categorized them as group borrower specific factors (i.e., peer monitoring, peer pressure, self-selection, homogeneity, group size, internal rule of regulation), lender specific

factors (i.e., loan size, training, experiences of credit officers) and socio-economic specific factor that affect principally the loan repayment rate of group borrowers.

Abreham (2002) studied on the loan repayment and its determinants in small-scale enterprise financing in Ethiopia around Zeway area. In an attempt to analyze the determinants of loan repayment status of borrowers and to identify the criteria employed to ration credit he used two equations; loan repayment and rationing equations. The estimation result employing Tobit model reveals that having another source of income, education, work experience in related economic activity before the loan and engaging on economic activities other than agriculture are enhancing while loan diversion, being the male borrower and giving extended loan repayment period is undermining factors of the loan recovery performance of projects. With regards to the loan rationing mechanism, he found that borrowers who secured high value of the collateral and those with relatively longer repayment period were favored although they tend to be riskier while those with higher equity share and extensive experience in related activity were disfavored.

Bekele et al. (2005) studied the socio-economic factors influencing repayment of agricultural input loan in Ethiopia using a logit model. The result of the model showed that total livestock holding, the amount of loan taken by households, off-farm income by a member of the household, yield loss, grain production and timeliness of input supply, became significant variables. Brehanu and Fufa (2008) employed probit and logit regression to study the determinants of loan repayment rates for agricultural loans among small-scale farmers in Ethiopia. In the study, they found that borrowers with larger farms, higher numbers of livestock and farms located in a rainfall area had a higher capacity to repay loans since all those factors increased the farmers' productivity and income. The study also found that borrowers who had extra business income and were experienced in using agricultural technology had a good repayment performance.

Belay (2002) employed a logit model to estimate the effects of hypothesized explanatory variables on the repayment performance of rural women credit beneficiaries in Dire Dawa, Ethiopia. Out of the twelve variables hypothesized to influence the loan repayment performance of borrowers, six variables were found to be statistically significant. Some of these variables are farm size, annual farm revenue, the celebration of social ceremonies, loan diversion, group effect and location of borrowers from the lending institution.

Gebrehiwot (2006) employed a logit regression model in his research and showed that five variables were significant to affect borrowers' loan repayment performance. These variables include the educational status of the sample household, family size of the household, duration of a cooperative member of the household, total size and use of land holding of the household and amount of money borrowed by the household. Except for the size of land holding, all the significant explanatory variables affect the loan repayment performance smallholders positively.

Million et al. (2012) studied factors affecting loan repayment performance of smallholder farmers in the east hararghe zone, Oromia, Ethiopia using a Tobit model. The result of the model showed that agro-ecological zone, off-farm activity, production loss, informal credit, a celebration of social ceremonies, number of contact days of the farm household head with extension agents and loan income ratio, determined repayment performance.

2.4. Conclusion and research Gap

Studies on loan repayment are not a new research area. In fact, various researches are conducted in loan repayment performance at a different time, but the results of findings are still debatable among different researchers. The finding shows there is Inconsistency empirical Findings, Lack of empirical studies specific to the determinants of loan repayment performance of borrowers in the study area of microfinance institution especially in OMFI and considering the facing financial constraints to sustain loan provision to the poor due to increasing in the default rate of the institution. Inconsistency of result regarding the determinant factor variables. Specifically, variables like Age, Gender, Education level, Method of lending and Loan size have debatable results. Therefore, in addition to solving the problems existed in the study area this study is going to fill the gap mentioned above by including additional variables on former researchers on determinants of loan repayment. Besides, as to the researcher's knowledge, it appears that no study has been conducted on microfinance loan repayment performance in Emdiber branch on urban and rural borrowers.

In addition to the above, other various studies were conducted on the determinants of loan repayment performance in different countries. Majority of the study conducted was focused on loan repayment related to rural borrowers, but few studies indicate loan repayment performance of urban borrowers. However, the present research focuses on the determinants of loan repayment performance of rural microfinance beneficiaries for the agricultural business, urban microfinance beneficiaries for commercial sectors, for the service sector, an enterprise sector and

Government employee microfinance beneficiaries the purpose of the loan was taken for household consumption rather than start the business or expanding the business. Furthermore, the study will also analyze the loan repayment performance of microfinance clients, the impact of lending on borrowers business activities, like commercial sectors, an enterprise sector which are involved in construction, metalwork, woodwork, kobil stone road construction and the like, service sectors and agricultural sectors on loan repayment performance of OMFI, that were not done by the other researchers before at the study area of OMFI. Therefore, this study aims at addressing this research gap.

CHAPTER THREE

3. RESEARCH DESIGN AND METHODOLOGY

3.1. Introduction

This chapter presents the methods and procedures that are followed in conducting the research with the aim of examining loan repayment and its determinants in the borrowers of Omo microfinance in Ethiopia, SNNPR, Gurage Zone, Emdiber city administration. The chapter discusses the research design, population, and sample, data collection techniques used, data analysis method that are employed in the study.

3.2. Description of the study area

Emdiber is a town in south-western Ethiopia. Located in the Gurage Zone of the Southern Nations, Nationalities and Peoples' Region, this town has a latitude and longitude of 8°7'N37°56'E / 8.117°N 37.933°E and an elevation between 2130 and 2164 meters above sea level. It is the administrative center of Cheha woreda, which is 182kms far from Addis Ababa, the capital city of Ethiopia. According to the Gurage Zone government, Emdiber is one of 12 towns with electrical power, one of 11 with telephone service and one of nine that have postal service. An all-weather road was built in 1963 by the Gurage Road Association, which connected Emdiber to Addis Ababa through Welkite and Hosaena.

Historically, in the early 1930s there was a Catholic mission of the Capuchins, usually with a Père and a Frère; they did some medical work and had a school. During the Italian occupation the mission was renamed "Missione della Consolata". The Emdiber market was held every Friday. In 1984 drought affected almost every household in Emdiber: there was no rain, and the *Enset* in many households was affected by a plant disease known as chire. Although it was insufficient, the community received aid in the form of clothes, maize, milk, butter and oil from the Catholic Relief Service, as well as some of the richer farmers in the area.

Demographically based on figures from the Central Statistical Agency in 2005, Emdiber has an estimated total population of 4,057 of whom 1,992 are men and 2,065 are women. The inhabitants practiced Ethiopian orthodox Christianity with 48.17 % of population, 42.32% were Muslims, 7.86 were Protestants and 1.34 was Catholics. Most of the people of Emdiber are speakers of Guragagna and Amharic.

3.3. Research Design

The study was employed explanatory research design with quantitative and qualitative methods to examine the determinants of loan repayment in Omo microfinance borrowers in Ethiopia Southern region, Gurage Zone, Emdiber city administration. The quantitative aspect of the data focused on the description of socioeconomic variables, loan, and related variables, and business-related variables and analysis of the relationship among the dependent and explanatory variables of OMFI for the study.

3.4. Target Population of the Study

The population for this study is borrowers of Omo MFI Emdiber branch are purposively selected. The number of borrower's data was collected from the borrower profile of the institutions. During the data collection period, borrowers would classify as defaulter and non-defaulter. The total target population of the study is 980 borrowers. The researcher used a total number of 8 officers (out of these 2 managers and 6 loan officers) are purposively selected for the interview in the study period.

Information obtained using the survey questionnaire includes:

- Borrower characteristics like age, sex, marital status, level of education, household size, occupation, etc.
- History of the loan (amount of loan, purpose, and utilization of loan, etc.)
- Information on group formation (group monitoring, group responsibility, group action, group member)
- Information on income (from activities financed by the loan and from other sources)
- Information like access to medical and educational facilities, nutritional status, etc.

Information on savings, Training and financial recording

- Information on business (Business experience, business type, business information, market study),
- Information on borrower's perception of the cost of default, customer service of the institution and other relevant variables and adequacy of supervision, and other relevant variables.

Information obtained from the branch office interview includes

- Information on loan like repayment period, loan term, loan disbursement and collection, availability of training, loan officers visits, and stability, etc, Information like screening mechanisms, saving services, the formation of groups/centers, etc.

3.5. Sampling Techniques and Sample Size Determination

3.5.1. Selection of Sample Respondents

The researcher used stratified sampling in selecting the representative's borrowers following the method of proportional allocation under which the sizes of the samples from different strata are relatively kept proportional to the sizes of the strata. The sample for this study consists of the defaulter and non-defaulter loan beneficiaries responding to the questionnaires. As per loan list survey, out of total 980 borrowers, 110 borrowers are a defaulter and 167 are non-defaulter borrowers. To develop the sampling size, lists of borrowers are acquired from the Emdiber branch microfinance borrowers profile list. A representative sample is selected from the total borrowers by using stratified sampling technique dividing the borrowers (population) into two strata, in terms of loan payment status as defaulters and non-defaulters. This study would be applied purposive sampling design to select the staff manager and loan officer respondents. It is because manager and loan officers are responsible for loan repayment performance and he/she was assumed to know the required information.

3.5.2. Sampling Procedure and Technique

Sample size determination formula was adopted to decide the sample size of borrowers for this study. The number of borrowers is 390 defaulters and 590 non-defaulters, totally the target study size will be comprised of 980 loan beneficiaries. To select a representative sample from this population, the numbers of borrowers are rural 569 and urban 411, totally the study size comprised of 980 beneficiaries, using the following scientific formula. First, the initial sample size is determined by using the following scientific formula:

3.5.2.1. The formula for Calculating a Sample for Proportions

For populations that are large, Cochran (1963:75) developed Equation 1 to yield a representative sample for proportions.

Equation..... (1) $n_o = z^2_{\alpha/2} * \frac{(p)(q)}{e^2} = 385$

Where Z= value for selected alpha level 0.025 in each tail (for 95% degree of confidence) =1.96, (p) (q) = estimate of variance = 0.25, e = the desired level of precision (i.e., the margin of error), p is the estimated proportion of the population which has the attribute in question, $q = 1 - p$. If the population is small then the sample size can be reduced slightly. This is because a given sample size provides proportionately more information for a small population than for a large population. The sample size (n_o) can be adjusted using Equation 2. Cochran's (1977) correction formula is used to calculate the final sample size. This calculation is as follows:

Equation..... (2) $n = \frac{n_o}{1+(n_o-1/N)} = \frac{385}{1+(385-1/980)} = 277$

Where “N” is the total population (980) and “n” is the sample size of the study. The researcher has selected 364 from borrowers as per stratified sampling. This sample size can be used as representative of the microfinance institutions “beneficiaries” because of borrowers under similar strata have homogenous characteristics and have a common environment in which they exposed to similar problems. Yamane (1967:886) provides a simplified formula to calculate sample sizes. This formula was used to calculate the sample sizes. A 95% confidence level and P = 0.5 are assumed for Equ.3.

To determine sample size from each stratum, the following sample size determination formula has been used:

Equation..... (3)
$$n_h = \frac{N_h}{N_s} * n \Rightarrow \left(\frac{390}{980}\right) * 277 = 110 \text{ Defaulter}$$

$$\Rightarrow \left(\frac{686}{980}\right) * 277 = 167 \text{ non - Defaulter}$$

Where: n_h = sample size from each stratum, N_h = Total population in each stratum, N_s =Total population of the sum of strata for study and n = Total sample size from the study population. The study will group in four sectors (Agricultural sectors, commercial sectors, enterprise sectors, and service sectors) according to the purpose of borrowing. The survey mainly purposely considers Emdiber branch only for the rural respondent are purposely selected in terms of their large number of clients.

Table 3.1: Proportionate sample size defaulter and non-defaulter borrower

Loan repayment status	Number of Borrowers					Proportionate sample size from stratum $n_h = \frac{N_h}{N_s} * n$	
	Urban		Rural		Total		
	1	2	3	4			
	Sample	PSS	Sample	PSS	1 + 3	n_h	2 + 4
Defaulters	166	47	224	63	390	(390/980)*277	110
None-Defaulters	245	69	345	98	686	(686/980)*277	167
Total	411	116	589	161	980	Total	277
Where; PSS= Proportionate Sample Size							

Source: survey result, 2021

3.6. Source of Data

3.6.1. Primary Data Sources

The primary data was collected from the sample of the branch's clients (both defaulters and non-defaulters) through a structured interview. The interview was made with key informants such as Loan Officers, Branch Manager, and Regional Coordinator to know the status of the portfolio quality of the Branch.

3.6.2. Secondary Data Sources

Secondary data was obtained from the branches annual progressive report. On top of these secondary data was gathered from the branches default register book.

3.7. Data Collection

The study was used both primary and secondary data which is obtained from Omo microfinance borrowers with the aid of questionnaires the questionnaire would be developed by the researcher and structured according to the objectives of the study. This would be used to generate information on the personal characteristics of the target group and to determine the factors affecting their repayment performance. Both closed and open-ended questions are used to obtain responses. The questionnaire is physically administered to each respondent, who was allowed enough time to respond. This study is conducted based on both primary and secondary data, using a structured questionnaire with the help of trained enumerators.

The primary data are collected by face to face interviews using a structured questionnaire. The questionnaire includes both closed and open-ended questions. The closed-ended questions used to collect background information about the respondent. It was covered the personal information,

institutional, group lending, loan, and repayment related questions. The open-ended questions deal with the challenges in the repayment process and institution, the perception of clients towards the OMF and microfinance institution as a whole.

The questionnaire was prepared in English language and then translated into local languages Amharic, the language spoken by the majority of the population in the study area.

In addition, qualitative data collected through semi-structured interview and discussions were made with selected loan officers and branch managers and relevant documents are reviewed. The questionnaire is pre-tested before conducting a survey for the whole sample. Secondary sources include published and unpublished materials about microfinance institution activities. Survey questionnaire would be revised and adopted from various related studies, Jemal (2003); Asmelash(2003); Fikirite(2011), Abraham(2013) and others. The questionnaire has mainly two sections, are divided into six main parts: such as a socio-demographic profile of borrowers, loan and loan-related questionnaires, group lending-related questions, business-related questions, institutional related questions, and other loan-related internal and external factors.

3.8. Data Analysis and Estimation Technique

For this study data analysis aims at satisfying the research objectives and provides a possible answer to the research question. For the survey collected data to be understood in an easy way, it needs to be analyzed.

The research used quantitative techniques in analyzing the survey data. After receiving questionnaires from the sample respondents the responses were edited, classified, coded and tabulated to analyze quantitative data using MS excel. Tables demonstrating frequencies and percentages were used for easy understanding and analysis. Finally, conclusions were made based on Chi-square (X^2) test results.

The empirical analysis of the study would be conducted using both descriptive statistics. Descriptive statistics discussion was made by using measures like percentages, tables, and maps used for comparing borrowers not paid credit/defaulters/ and paid credit/ non-defaulters /in various explanatory variables. Chi-square test was used for comparing defaulter and non-defaulter borrowers in various explanatory variables. The chi-square test is used to determine whether frequency distributions differ significantly. When using X^2 we first prepare a cross-

tabulation of the variables. The chi-square test can be applied to the cross-tabulation to determine whether there was a significant difference between distributions (Fisher and Foreit, 2002).

3.9. Definition of Variables

3.9.1. Dependent Variable

The dependent variable was the estimated result of the independent variable being operated and whose value depends on the value of independent or explanatory variables. It measures to demonstrate the effect of the independent variable. In this study, the dependent variable is loan repayment (LR) for the n^{th} borrowers (If $LR_n = 1$, borrowers, repaying the loan on time and $LR_n = 0$, borrowers do not repay the loan on time). The borrowers that did not repay the amount of money they borrowed as per credit schedules are considered as defaulters (denoted by is zero). Likewise, borrowers that repaid the amount they borrowed per credit schedules are considered as non-defaulters denoted by one.

3.9.2. Independent Variables

The independent variable was normally the variable indicative of the value being manipulated or changed and used to explain the dependent variable. For the purpose of this study, the researcher would be included 16 independent variables as summing that it is best to explain the determinants of loan repayment performance of OMF borrowers. Performance of Loan Repayment Determinants in OMF Borrower - An Analysis

CHAPTER FOUR

4. DATA ANALYSIS, PRESENTATION AND INTERPRETATION

4.1. Introduction

This chapter describes the interpretation and explanation of the findings of the research that are in line with the research question and objectives of the study. To achieve the above mentioned both descriptive and inferential statistics were used to respectively summarize and draw conclusions on the data.

4.2. Questionnaires Response Rate

Of the 277 questionnaires distributed, 260(94%) were returned dully filled, and 17(6%) were returned incomplete. A section of respondents was uncomfortable with the information that put them in bad light or in their view was private and confidential. This category of respondents, for instance, skipped questions on why they defaulted on the loan repayment, or their other sources of income if any. Altogether the 94% response rate through low still is within the acceptable threshold, of course notwithstanding the fact that there seems to be a lack of consensus across disciplines on the question of acceptable response rate in research. The above-indicated response rate (96%) according to Mundy (2000) lies within reasonable margins, although not inside the brackets of what would be considered as good (80%) or excellent (90%). However going by the acceptable thresholds provided by Mugenda and Mugenda (2003), the above-given response rate of 94% lies with excellent margins (90 and above).

4.2.1. Demographic Characteristics and Loan Repayment Performance

According to these section respondents demographic Characteristics are presented as shown in the table below and the statistical significance of each discussed. Among the characteristics discussed include: Age of the borrower, Educational level of the borrower, marital status, of the borrower, Family size of the borrower, Location of residence, other sources of Income, and Celebration of social ceremonies.

Table 4.1: Demographic characteristics of respondents

Variables	Category	Frequency	Percentage
Age of Borrower	20-30 Years	26	10%
	31-40 Years	100	38.5%
	41-50 Years	92	35.2%
	Above 51 Years	42	16.2%
Marital Status	Married	158	60.8%
	Single	102	39.2%
Educational Level	Illiterate	30	11.5%
	Grade 1-8	72	27.7%
	Grade 9-12	93	35.8%
	Above Grade 12	65	25%
Location of residence	Urban	109	41.9%
	Rural	151	58.1%
Family Size	0-3	128	49.2%
	4-6	113	43.5%
	Above 6	19	7.3%
Other Sources of Income	Agriculture-type sources of income	140	53.8%
	Business type sources of income	93	35.8%
	Monthly Salary or pension	27	10.4%
Celebration of Social Ceremonies	No	160	61.5%
	Yes	100	38.5%

Source; Field Survey Result 2021

Table 4.1 in the above showed the distribution of respondents according to socio-economic characteristics. The majority (38.5%) of the respondents were within the age range of 31 - 40 years, whereas 35.4%, 16.2% and 10% were within the age brackets of 31 – 40, 41 – 50, above 51 and 20 - 30 years respectively. The implication is that youths dominated the sampled borrowers in the study and according to literature, this age class has common features of being motivational, risk-averse and adoptive individual for enhanced production and less prone to loan defaulting (Ibrahim and Aliero, 2012). However, this finding contradicted the works of Njoku, (1997) who opined that aged people are more trust worthy to live up to their promises of loan repayment than younger ones.

Table 4.1 revealed further that most of the respondents were married and accounted for about 60.8% of the total sampled borrowers. This was followed by a single (39.2%). Married people as asserted by Anozie, et al. (2014) are likely to incur extra expenditures for family livelihood from the loan, thereby threatening their loan repayment ability. Also, the majority (49.2%) of the respondents had household sizes of 0- 3, while the least (7.3%) had above 6 people. Large household size could be a source of cheap family labor especially during the peak of agriculture activities when the cost of hired labor is high. In this aforementioned scenario, such household head will have a high propensity to save lots of money that could have been used for hired labor and use it offset his/her loan (Kedir, 2007). In contrary, Ibrahim and Aliero, (2012) opined that large family size that comprises more of dependent population, the household head have more probability of being loan defaulters as such loan are often diverted to family welfare upkeep (Adams, 1998).

In addition, the majority (35.8%) of the respondents were educated, while only 11.5% were not educated. An educated borrower has the potentials of enhancing their agriculture and other business productivity and economic status through the adoption of new technologies. The money accruing from the sales of his/her outputs could be used to compensate for the loan (Osuntogun, 2012).

4.2.2. Demographic and Socio-Economic Characteristics

The demographic distribution, socio-economic characteristics and institutional characteristics of the respondents such as gender of the borrower, age of the borrower, marital status, method of lending, level of education, family size, loan size, loan repayment schedule, availability of training, loan supervision and advisory visits, distance from Omo microfinance service center, other sources of income, business experience, celebration of social ceremonies, external shock, voluntary saving and other variables related to loan repayment (defaulters and non-defaulters) were analyzed using descriptive statistics. In this study, from the total population of 980 Omo microfinance borrower, 277 samples of borrowers were interviewed from selected six Kebeles (4 rural and 2 urban) of the Emdiber City Administration. According to the survey result, the total number of borrowers in sample 126 (45.49%) are from the urban borrowers and 151 (54.51%) are from the rural borrowers of OMFI. From the total sample respondents, 194(74.61%) are non-defaulter while 66(25.39%) defaulters beside this, from the total respondents only 99(38.08%) of the total sample are female, the rest 161(61.92%) are male.

4.3. Performance of Loan Repayment by Each explanatory Variable

As tabulated table 4.2 below, among the 260 sample respondents, majority 100(38.5%) of loan borrower lie in the 31-40 years age, followed by 92(35.4%), 41--50 years age, 42(16.2%) above 51 years age and 20-30 years 26(10%) in that order. A further investigation into the repayment rate of each age bracket was carried out and the results are as follows. As the table data indicated that the loan borrowers of age group 31-40 years, 41-50 years and above 51 years age each with the default rate of 11.9%, 17.7% and also 6.9% respectively have the highest default rates compared to those in the other age brackets that are 20-30 years 5.8%. Since there were only conclude that emerged the best loan payer's 5.8% default rate, although notably, this group is so small that it is unfeasible to make a concrete conclusion on its traits. Overall, the association between loan repayment performance and age group was found to be statically significant with Pearson Chi-square 9.995.

Table 4.2: Performance of Loan Repayment by Age of Borrower

Age of the borrower :- Loan Repayment Performance Cross tabulation						
How old are you on your last birthday?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Age of the borrower	20-30 Year	Count	15	11	26	9.995
		% of Total	5.8%	4.2%	10.0%	
	31-40 Years	Count	31	69	100	
		% of Total	11.9%	26.5%	38.4%	
	41-50 Years	Count	46	46	92	
		% of Total	17.7%	17.7%	35.4%	
	Above 51 Years	Count	18	24	42	
		% of Total	6.9%	9.2%	16.1%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

On marital status, the survey indicated that the majority of sample respondents 158(60.80%) are married, while 102(39.20%) are single. The low number of single clients can be attributed to a many of reasons including minimal financial obligation, luck of physical collateral, not being a

member in an organized group, or even possibility that they are denied loans due to their less predictable geographical mobility which increase loan collection risk.

Table 4.3: Performance of Loan Repayment by Marital Status

marital status of borrower :- Loan Repayment Performance Cross tabulation						
What about your marital status?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
marital status	Marred	Count	37	121	158	58.878
		% of Total	14.2%	46.5%	60.8%	
	Single	Count	73	29	102	
		% of Total	28.1%	11.2%	39.3%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100.0%	

Source; Field Survey Result 2021

Table 4.3 above gives an overview of loan repayment performance and marital status. According to the below table 4.3 comparing the married and single it is notable that while the 73(28.1%) of single defaulted only 37(14.2%) of the married defaulted on the contrary from the sample respondents 121(46.5%) of the married non-defaulter, 29(11.2%) of the single non-defaulter. This implies that the married borrowers are better on loan repayment performance possibly as proposed by Haile (2015), the married have more access to information and resources, and hence higher loan repayment capacity. These findings present the single as a higher risk group in loan repayment compared to the married. Nonetheless, there is a possibility that the results of loan repayment and marital status could be done to mere chance. This conclusion is informed by a Pearson chi-square test 58.875.

Table 4.4: Performance of Loan Repayment by Method of Lending

Method of Lending:- Loan Repayment Performance Cross tabulation						
What is your Method of Lending?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Method of Lending	Group	Count	30	124	154	75.360
		% of Total	11.5%	47.7%	59.2%	
	Individual	Count	80	26	106	
		% of Total	30.8%	10.0%	40.8%	
	Total		Count	110	150	260
			% of Total	42.3%	57.7%	100.0%

Source; Field Survey Result 2021

Under this section, as the test statistics show Table 4.4 above method of borrowing is significant at less than 1% level the result shows that for the group and individual borrowers there was a different result in the defaulter and non-defaulter. On the basis of method of borrowing, from the total sample respondents the majority 124(47.7%) group borrowers were non-defaulters and 30(11.5%) were defaulters, while individual lending from the total sample size 26(10.0%) were non-defaulters and 80(30.8%) were defaulters (Table 4.4). Regarding the loan repayment status of the clients, from this result in terms of loan repayment status group borrowers are better than individual borrowers to pay the loan successfully. This result also indicated to ensure repayment, peer pressure and joint liability work very well especially in the rural-urban area.

Table 4.5 Performance of Loan Repayment by Educational level

Educational level of borrower :- Loan Repayment Performance Cross tabulation						
What about your level of Education?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Educational level of borrower	Illiterate	Count	0	0	30	179.227
		% of Total	0.0%	11.5%	11.5%	
	Grade 1-8	Count	66	6	72	
		% of Total	25.4%	2.3%	27.7%	
	Grade 9-12	Count	0	93	93	
		% of Total	0.0%	35.8%	35.8%	
	Above Grade 12	Count	44	21	65	
		% of Total	16.9%	8.1%	25.0%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

According to the level of Education, table 4.5 above indicates that out of the total sample respondent majority of respondent 30(11.5%) have never attended secondary school, a revelation which raises the question of the ability of such respondents to understand training on loan terms, loan obligations and calculation of remaining balance after each payment. Unless one is able to understand and perform the necessary calculations indicated above, doubt is cast on his literacy. Going by the definition of UNESCO (2006), “a person is literate when he can engage in all those activities in which literacy is required for effective functioning of his loan group and community

and also for enabling him to continue to use reading, writing, calculation for his own and the community's development." In view of the above-stated definition, in the research persons who did not attend secondary school education were treated as functionally illiterate particularly in the area of manipulated skill. The above explanation all about the illiterate Omo microfinance clients but the study data was split in to illiterate, Grade 1-8, Grade 9-12 and Above Grade 12. The repayment rates of the four groups are as indicated in table 4.5 above. The table below shows that out of the total sample respondents (260)- 30, 72, 93 and 65 were functionally illiterate, Grade 1-8, Grade 9-12 and above Grade 12 respectively, both Grade 1-8, and above grade 12 defaulted by 66(25.4%) and 44(16.9%) respectively defaulted and the remaining that means the illiterate and Grade 9-12 0(0%) defaulted. Overall, the results posted a Pearson Chi-square 179.227 leading to the conclusion that there is a statistically significant association between education level and loan repayment performance. This confirms the perspective of the opinion of Gebremedhin (2010) that higher education level enables borrowers to comprehend more complex information, keep business, records, conduct basic cash flow analysis, and make the right business decision. Hence, borrowers with a higher level of education may have higher loan repayment rates rather than the lower level.

Table 4.6: Performance of Loan Repayment by Location of residence

Location of residence:- Loan Repayment Performance Cross tabulation						
Location of your residence?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Location of residence	Urban	Count	66	43	109	25.590
		% of Total	25.4%	16.5%	41.9%	
	Rural	Count	44	107	151	
		% of Total	16.9%	41.2%	58.1%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100.0%	

Source; Field Survey Result 2021

According to table 4.6 above, On the basis of the location of residence, 16.5% urban borrowers were non-defaulters and 25.4% were defaulters, while rural borrower 41.2% were non-defaulters and 16.9% were defaulters. From this result, in terms of loan repayment status, rural borrowers are better than urban borrowers.

Table 4.7: Performance of Loan Repayment by Family Size Borrower

Family Size Borrower:- Loan Repayment Performance Cross tabulation						
What about your level of Education?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Family Size Borrower	0-3	Count	61	67	128	38.907
		% of Total	23.5%	25.8%	49.2%	
	4-6	Count	30	83	113	
		% of Total	11.5%	31.9%	43.5%	
	Above 6	Count	19	0	19	
		% of Total	7.3%	0.0%	7.3%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

According to family size, Children are often viewed as consumers, not producers. As such, family size becomes an important demographic characteristic to weigh in that persons with bigger families are more likely to seek credit services due to many financial demands of the individual members thereof. Similarly, it would be expected that often than not such clients will default more considering that their earnings may not competition the many demands of the large family. An added financial obligation will only make an already bad situation worse. The findings indicated that most sample respondents 128(49.2%) had 0-3 children followed by those with 113(43.5%) had 4-6 children. Those with 19(7.3%) had above 6 children. Table 4.8 below tabulates the loan repayment rate of each individual category. From the table 4.7 above considering each group separately, comparing the group, those with 19(7.3%) had above 6 children are likely to default more than those with 113(43.5%) had 4-6 children and 128(49.2%) had 0-3 children as indicated by their comparative default percentage of 28.8%, 0%, and 36.7% respectively. It is surprising that clients with 0-3 children defaulted more 49.2% than those with 4-6 children (43.5%). Possibly there is a chance that the latter (those with 4-6 children) have fewer dependents considering that some of the children may already be working and contributing toward loan settlement among other financial obligations. This perspective consistent with the finding of Wonganaa and Victor (2013), however, considering the data without regarding specific instances, overall there is no pattern suggesting that successful loan performance

dependents on a number of children. It is no wonder that the goodness of fit statistics gave a Pearson chi-square 38.907.

Table 4.8: Performance of Loan Repayment by Loan size

Loan size of Borrower:- Loan Repayment Performance Cross tabulation						
Did you receive the amount you had requested?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Loan size of Borrower	Up to 5000	Count	93	20	113	134.413
		% of Total	35.8%	7.7%	43.5%	
	5001-10000	Count	3	71	74	
		% of Total	1.2%	27.3%	28.5%	
	Above 10000	Count	14	59	73	
		% of Total	5.4%	22.7%	28.1%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

According to table 4.8 above the loan size out of the total sample borrower was 113(43.5%) up to 5,000birr Loan size, the second 74(28.5%) from 5001-10,000 birr loan size, the last and the third one is 73(28.1%) above 10,000 birr loan size. From this 93 sample, respondents are defaulter up to 5000birr loan size, 74 sample respondents are non-defaulter from 5001-10,000birr loan size and 91 sample respondents are non-defaulter above 10,000 birr loan size. From this study the researcher implied the loan size of the clients increase better to run the business activity and expand the existing business or start the new business as well finally paid the loan successfully. This conclusion is informed by a Pearson chi-square test 134.413. This statistic result indicates or shows that there is an association between Loan size and loan repayment performance.

Table 4.9: Performance of Loan Repayment by Timelines of Loan Released

Timelines of Loan Released:- Loan Repayment Performance Cross tabulation						
Loan released on time?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Timelines of Loan Released	Was not Timely Released	Count	66	69	135	4.983
		% of Total	25.4%	26.5%	51.9%	
	Was Timely Released	Count	44	81	125	
		% of Total	16.9%	31.2%	48.1%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

From table 4.9 above Timelines of Loan Released refers to as loans which are disbursed on the right time or not to the microfinance borrower. The table or the MS excel output results show from the total sample respondents 135(51.9%) said was not timely loan released, from this 66(25.4%) defaulted and 69(26.5%) non-defaulted. From the total sample respondent, 125(48.1%) respondents said the loan was timely released, from this 44(16.9%) defaulted and 81(31.2%) non-defaulted. The result shows the Omo microfinance was not timely released the loan to the borrower due to these the defaulted rate is higher than the non-defaulted rate. This conclusion is informed by a Pearson chi-square test 4.983. This statistic result indicates or shows that there is an association between Loan diversion and loan repayment performance. This implies the amount of loan released was not timely released for the borrower. The loan has a positive impact on the borrower's capacity to repay.

According to table 4.9 above comparing the Timelines of loan released, 135(51.9%) the loan was not timely released, from this 66 (25.4%) defaulted and 69 (26.5%) non-defaulted. according to timely released 125(48.1%), the loan was timely released, from this 44(16.9%) defaulted and 81(32.2%) non-defaulted. As per the response on the timeliness of loan release, 51.9% and 48.1% replied was not timely released and was a timely released answer respectively. The difference between the two groups was statistically significant at less than 5% level. That means Chi-square is 4.983. It is so rights to submit that there is a statistically significant association between loan repayment performance and marital status.

Table 4.10: Performance of Loan Repayment by Loan Repayment Schedule

Loan Repayment Schedule:- Loan Repayment Performance Cross tabulation						
Did you think that the loan schedule is appropriate for you to pay back?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Loan Repayment Schedule	Otherwise	Count	106	98	204	137.541
		% of Total	40.8%	37.7%	78.5%	
	Suitable	Count	4	52	56	
		% of Total	1.5%	20.0%	21.5%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

This section presents and discusses findings on the association between loan repayment schedule and loan repayment performance. Two repayment schedule aspects were considered, one is the suitability and the other one is unsuitability of the loan repayment schedule.

According to Table 4.10 above from the total sample respondents 56(21.5%) are suitable and 204(78.5%) unsuitable loan repayment schedule from the total 260 unsuitable 106(40.8%) defaulted and 98(37.7%) non-defaulted and the next suitable 52(20.0%) non-defaulted and 4(1.54%) are defaulted. The loan is not successfully paid, this shows the default rate will be high and the non-default rate is low.

Table 4.11: Performance of Loan Repayment by Availability of Training

Availability of Training:- Loan Repayment Performance Cross tabulation						
Did you get any training before receiving the loan?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Availability of Training	No	Count	37	58	95	0.693
		% of Total	14.2%	22.3%	36.5%	
	Yes	Count	73	92	165	
		% of Total	28.1%	35.4%	63.5%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

The study, however, found out that training, which has been built into supervision programs of the institution including visitation in homes, business premises, and small groups does not impact loan repayment. This judgment is based on the results posted in table 4.11 above. One would have expected the default rate between those who were trained and otherwise to be significantly different. However, as shown in table below, the default and non-default rate among the borrower is different. Out of 260 respondents, 165(63.5%) were trained and 95(36.5%) were not trained. Among those who were not trained, 110(42.3%) unsuccessfully repaid their loans while 150(57.7%) of those trained repaid loan successfully. This narrow variation is reflected by the Pearson Chi-square test result of 0.693, meaning that there is no probability that there is a statistically significant association between availability of training and loan repayment performance. Interpret further, this means that there is a 40% possibility that the above-stated results could occur by chance or put differently as a result of random distribution. This finding is confusing and contrary to the findings of other researchers including Yunus (2016). Several factors, however, can explain away this state of affairs. To begin with, in spite of the provision of training, the poor are many times, especially during famine seasons, extremely pressed by immediate consumer needs that no training will persuade them not to borrow even when natural knowledge tells them that it is unwise to do so. Secondly, unless training is relevant, on target, addressing the real issue in real time, it is less than helpful. Thirdly, earlier in the study, it was discovered that most of the respondents were functionally illiterate.

Table 4.12: Performance of Loan Repayment by Loan Supervision and Advisory Visited

Loan Supervision and Advisory Visited:- Loan Repayment Performance Cross tabulation						
Have you ever been supervised for Loan Repayment by OMFI staffs?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Loan supervision and advisory visits	No	Count	110	86	196	62.259
		% of Total	42.3%	33.1%	75.4%	
	Yes	Count	0	64	64	
		% of Total	0.0%	24.6%	24.6%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

Table 4.12 above shows the adequacy of Loan supervision and advisory visits made by loan officers to groups and individual clients, to reduce the default rate and also maximize the non-

defaults rate. The table below shows, from the total sample respondents 196(75.4%) inadequate supervision and 64(24.6%) adequate supervision and visited. These indicated the microfinance officers do not supervise and visited the clients sufficiently or adequately, from this the result represents there is a high default rate and low non-default rate. The chi-square test carried out for the frequency of visits by loan officers revealed a chi-square statistics of 62.259. This statistic result indicates or implies that visitation may assist borrowers to get regular consultation and follow up to strengthen their income generating activities there is a strong relationship between Loan supervision and advisory visits and Loan repayment performance.

Table 4.13: Performance of Loan Repayment by Other Sources of Income

Other Sources of Income:- Loan Repayment Performance Cross tabulation						
What are the main sources of your family income?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Other Sources of Income	Agriculture-type sources of income	Count	39	101	140	49.750
		% of Total	15.0%	38.8%	53.8%	
	Business type sources of income	Count	44	49	93	
		% of Total	16.9%	18.8%	35.8%	
	Monthly Salary or pension	Count	27	0	27	
		% of Total	10.4%	0.0%	10.4%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

According to table 4.13. above, the regression result shows from the total sample respondents 140(53.8%) agricultural type sources of income, the next 93(35.8%) business type sources of income and the last 27(10.4%) monthly salary or pension sources of income. The association between other income sources which were not financed by the business and loan repayment was negative indicating that borrowers who had no other alternative source of income were found to be not better payers relative to those who did have other sources of income.

Table 4.14 Performance of Loan Repayment by Celebration of Ceremonies

Celebration of Ceremonies:- Loan Repayment Performance Cross tabulation						
Did you celebrate social ceremonies in 2020/21 fiscal year?			Loan Repayment Performance		Total	Chi-square
			Defaulters	Non-Defaulters		
Celebration of Ceremonies	No	Count	110	50	160	158.836
		% of Total	42.3%	19.2%	61.5%	
	Yes	Count	0	100	100	
		% of Total	0.0%	38.5%	38.5%	
Total		Count	110	150	260	
		% of Total	42.3%	57.7%	100%	

Source; Field Survey Result 2021

As of the study celebration of social ceremonies includes like wedding, religious festivities, funeral, and happy birthday and engagement. According to table 4.14 above, from the total sample, 160(61.5%) has not celebrated any social ceremonies at their village while 100(38.5%) has celebrated at least one social ceremony. 150(57.7%) of non-defaulters were not celebrating any ceremonies while and use the loan for the intended purpose. 110(42.3%) of the defaulters celebrated social ceremonies during the last two years. This shows the intended loan diverted to for consumption or unintended purposes. The result showed that the average amount of money spent on social ceremonies was smaller for defaulters than non-defaulters. As expected, social ceremonies have not affected the loan repayment rate negatively and significantly, Pearson Chi-square 158.836. Each additional unit spending on social ceremonies decreased the loan repayment by 0.220. The result of this study was in complete agreement with the result obtained by Belay (1998).

4.4. Internal and External challenges of the institution

The most typical challenges faced by any microfinance institution are a credit risk. Moreover, the cost of debt collection per loan amount is, on average, higher than in formal intermediation, especially in developing countries lending (Vento 2004). In addition to this OMFI as an institution have many internal and external challenges, such as internal challenges:

According to branch manager currently, OMFI is facing internal and external problems. Some of the internal problems are - Shortage of loanable funds for further expansion, High turnover of employees to other organizations, they are mainly attracted by better salary scales and benefits provided by these organization. Compared to the government organization salary scale of the

institution is higher. But the problem is that OMFI's employees are attracted by the private commercial banks and NGOs, there is not enough employees in the institution specially loan officers, all activities in the institution done manually /don't use computerized system insufficient working place/office in most of service delivery posts, staff of the institution where share one office with the employees of other government organization, Poor documentation

External challenges: Competition- there is very strong competition faced with conventional banks in mobilization of savings and increasing withdrawal. People trust formal banks especially commercial bank of Ethiopia. Moreover, the other sources of competition are NGO's, women's fund and other institutions who give loan without interest, improper interference of the third party in the decision of loan approval. In this regard, Norell (2001) also reported that if the loan is given without the proper evaluation of the business, the default rate may increase.

According to Sub Branch managers the most typical challenges faced by any microfinance the institution is; - activities in the institution are done manually or without an available computer access, not enough employees in the institution mainly in the loan department, borrowers think the loan as government gift and giving false certification for borrowers in Kebeles level (without considering the ability to pay)

According to Loan officer say that "In my opinion, one of the factors which affect loan repayment performance is the lack of motivation of workers. I am working in this office more than three years in my stay time; there is no salary improvement as well as scholarship chance. Even if this institution does not apply BSC, so our future is not good. So we are not volunteers to collect and provide service according to standards, no measurement at all. In addition to this, no training is given by the institutions and workload on the employee. During my supervision time, some borrowers believe loan as a gift of government, have no plan to repay and they ask loan without lending interest rate".

Table 4.15 Institutional Factors by the respondent

Institutional Factors	Rural	% age	Urban	% age
Shortage of loan able fund	21	14	8	7.27
Poor knowledge of loan officers	22	15	11	10
Weak in honest of loan officers	11	7.28	6	5.50
Un availability of grace period	23	15.33	18	16.51
Insufficient training is given by the institutions	23	15.33	14	12.84
They do not provide the necessary information like interest rate	11	7.28	8	7.27
Poor customer handling especially the manager of the services delivery center	18	11.92	14	12.84
Weak in following up to retrieve loans and on business	4	2.65	16	14.68
Third party services tend to interfere with their primary services because employees, become busy especially the cashier	17	11.26	15	13.76
Total	150	100	110	100

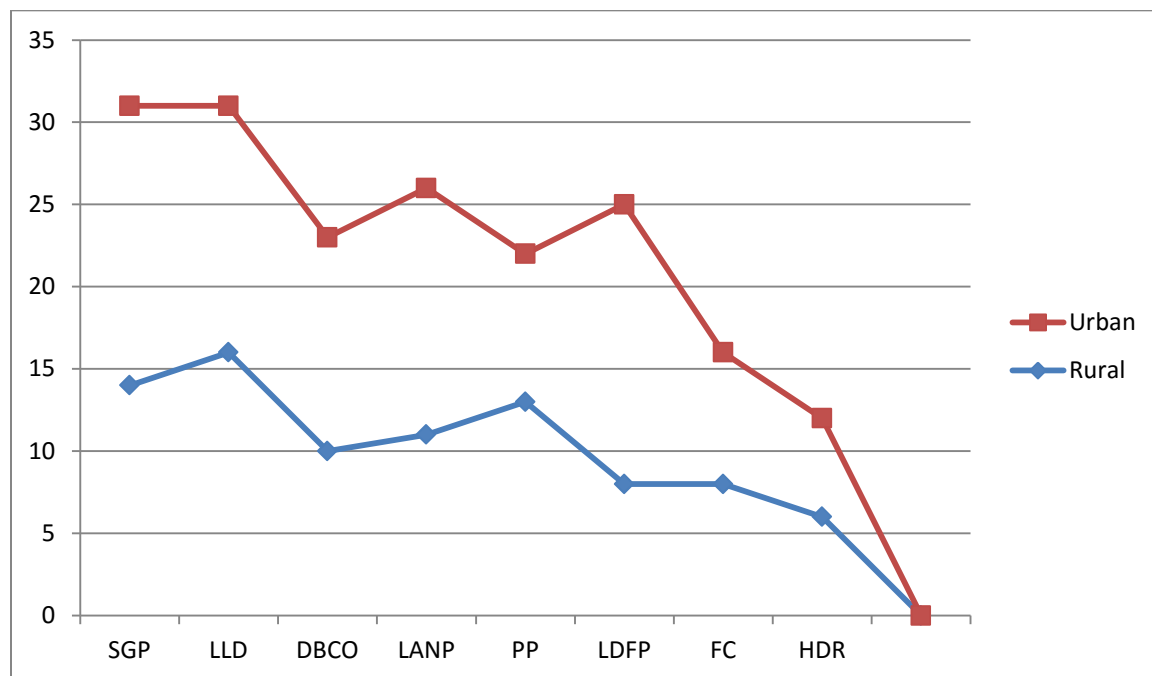
Source; Field Survey Result 2021

Table 4.16 Borrower's Responses on Main Reasons for Default

Reasons For Default in Urban and Rural	Defaulters In Urban and Rural (83)				
	Rural (47)		Urban (36)		Total
	In No.	In %	In No.	In %	
Due to Shortage of grace period (SGP)	9	14	8	17	17
Lag of loan disbursement (LLD)	10	16	7	15	17
Diverting borrowed capital to other (DBCO)	6	10	6	13	12
Loan activity was not profitable (LANP)	7	11	7	15	14
Personal problem (like sick) (PP)	8	13	4	9	12
Lack of demand for production (LDFP)	5	8	8	17	13
Family celebration (wedding, birth, etc (FC)	5	8	4	8	9
Due to high deduction rate(Service charge, Involuntary saving, and other miscellanies deduction) (HDR)	4	6	3	6	7
Total	63	100	47	100	110

Source; Field Survey Result 2021

Figure 1: Borrower's Responses on Main Reasons for Default



CHAPTER FIVE

5. SUMMARY OF FINDINGS, CONCLUSION, AND RECOMMENDATION

5.1. Introduction

This chapter presents conclusions and recommendations based on the analysis made in the previous chapter. The chapter will focus on the meaning of the findings, what actions should be taken in light of the results. It will be presented here whether the findings in general or in part confirmed the hypothesis and how they related to the objectives of the study which as indicated in chapter one where, establishing the influence of demographic characteristics, institutional characteristics and Socio-economic characteristics on loan repayment performance. At the end of the chapter, recommendations for policy and suggestions for further research will be presented.

5.2. Summary of Finding

Now a day, poverty becomes a major problem in many developing countries. In these countries, poverty is severed which has left millions of people out of basic needs for survival.

In Ethiopia, there are many poor people living in rural and urban areas. The accessibility of financial services plays an important role in creating self-employment opportunities for the majority of the low-income population.

The main problem of the weak performance of financial institutions in many developing countries is the high rate of non-repayment of the loan. The default rate of Omo microfinance institution is increasing from time to time. This study was intended to identify the determinants of loan repayment performance of Omo microfinance institution in Emdiber branch.

In spite of the key role that microfinance plays, its acquisition and repayment are fraught with a number of problems, the major being loan default. Factual to this assertion, from the total sample respondents of 277 borrowers, the study found out 47(16.97%) defaulter and 69(24.90%) non-defaulter sample urban borrower and 63(22.74%) defaulter and 98(35.38%) sample rural borrowers, totally 110(39.71%) of sample respondents did not promptly repay their loans that means defaulted respondents. At the beginning of the research the three characteristics, demographic characteristics, institutional characteristics, and Socio-economic characteristics, were hypothesized as contributing to this high rate of default.

5.3. Conclusions

According to the study, this research paper examines the demographic, socio-economic and institutional problem of Determinants of Loan Repayment Performance in Microfinance Institutions: in Case of Omo Microfinance (OMFI) In Emdiber branch. For the analysis purpose descriptive method were employed.

According to the outputs of age, education level, family size, loan size, loan diversion, loan repayment schedule, loan supervision and advisory visited, and celebration of social ceremonies are positively related to loan repayment performance, whereas timelines of loan released, and other sources of income have negative association with loan repayment.

This study similarly evidenced that, other variables such as marital status, method of lending, location of residence; voluntary saving and availability of training were not significant determinants of loan repayment performance of borrower's Omo Microfinance institutions.

Microfinance has been accepted not only as a financial mean to target specific people who excluded from the formal financial system to gain access to sources of financing, but it understands also a social aspect contributing to poverty reduction, women empowerment, economic development, and employment creation.

In order to survive negative shocks and maintain good financial stability, the financial managers and policy maker should identify the key loan repayment performance determinants of OMFI. Because of this, the current study uses both primary and secondary data to investigate the repayment performance of OMFI and repayment determinants on the loan repayment performance of OMFI.

To attain this objective the researcher began by reviewing the literature, also applied to unite theories in order to test theories and then identified factors affecting loan repayment performance that could apply to the empirical data.

The uniting theory was important for joint liability in the repayments of microfinance loans. The aim of this theory is to improve repayment rates and the welfare of credit-constrained borrowers. In joint liability, when one borrower cannot repay a loan, group members are responsible to repay for one of their members if he or she defaults to pay for his or her monthly installment.

After collecting this data, the researcher formed a basic sample of 277 OMFIs borrower in Emdiber branch. Subsequently, the researchers processed and analyzed the data gathered and clarify the determinants of loan repayment performance of OMFIs in Emdiber branch.

Therefore it can be concluded that age group above 31 years, higher education level, large family size, timely loan released, loan diverted to intended purpose, suitable loan repayment schedule, adequate loan supervision and advisory visited, large amount of loan applied or loan size, agriculture and business type sources of income, celebration of social ceremonies without loanable fund, low external shock and longer duration of business result in increased loan repayment and vice versa.

However an increase in married borrowers, individual method of lending, urban location of residence, decreasing voluntary saving and decreasing availability of training leads to more loan default and vice versa.

5.4. Recommendations

- ✓ The concerned body should have clear and effective credit or lending policies and procedures and must be regularly reviewed.
- ✓ The concerned body especially the credit supervisor should check with credit officers daily to ensure that policies are followed and the supervisor must respond quickly to solve credit officers' problems.
- ✓ The researcher recommends to the concerned body to show the direction in order to use ICT/core banking system to microfinance institution for effective and efficient financial services to the clients.
- ✓ The researcher recommends to the concerned body that to create an enabling environment by lowering the interest rate and by supporting microfinance institution with credit to lend to its members.
- ✓ Recommend the concerned body to minimize the default rate should be Quick follow-up after a missed payment, Regular visits to homes and businesses of clients, Adequate and proper appraisal, Proper client selection, and Group lending, use of third-party guarantee among others are the major measures to control or minimize default/delinquency.
- ✓ Recommend the concerned body to design strong strategy for control or minimize default/delinquency by categories the clients as willing and able to repay, willing but unable to repay, unwilling but able to repay, and unwilling and unable to repay.

- ✓ Recommend the lender institution considering to enhance post-disbursement monitoring system, technical assistance given to the microfinance recipients, to assign experienced field workers, Establish a common or provide common accessible database of the microfinance recipients, purchasing of equipment and limit the amount of cash disbursement, provide Strong training system for recipients and field workers of MFIs, Motivational programs for recipients, Motivational programs and salary increment for staff worker in order to reduce employee migration.

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APPENDIX
Wolkite University
Faculty of Business and Economics
Department of Accounting and Finance
Questionnaires to be Filed by OMFIs Beneficiaries

Dear Respondents;

I am a graduate student at Wolkite University. Currently, I am doing a research on ***“Determinants of Loan Repayment Performance in Microfinance Institutions: Case of Omo Microfinance Institutions (OMFI) in Emdiber”*** as a reference. The research is purely for academic purpose and your response is completely anonymous, but your views, in combination with those of others, are extremely important.

Thus the following questions are for analytic purposes only. It will not be used to try to identify any individual and/ or to attack the dignity and reputation of Beneficiaries.

“Thank you for devoting your precious time to complete this questionnaire”.

PART I:- Socio-Demographic Characteristics

Direction:- For the following items please mark ‘√’ or ‘x’ on the one which suits your response

1. Sex of borrower’s Male ☐ Female ☐
2. Age of borrowers’: 18-24 ☐ 25-28 ☐ 29-35 ☐ 36-46 ☐ Above 46 ☐
3. Educational background of borrowers’
Primary High school ☐ High school graduate ☐ Diploma ☐ First Degree ☐
Second Degree and above ☐
4. Marital status of borrowers’:- Single ☐ Married ☐ Widowed ☐ Separated ☐
5. Head of the Household:- Male ☐ Female ☐
6. How long have you been a member of the microfinance institution? Month____year____E.C
7. How many persons in your household (those who are live together with you and share the same food at least once in a day?)
 - a) Children less than 17 years of age/younger:- ☐ Male____ Female____ Total____
 - b) Adult above 18 years of Age or older:- ☐ Male____ Female____ Total____

8. How many persons in your household are working engaged in work that earns income or products? Male___ Female___Total_____

PART II:- Loan and Loan Repayment Related Questions

- 1) Did you have other source of income (cash income) before joining the loan program?
Yes ☐ No ☐
- 2) If your answerer in #1 is “yes” what is/are your sources of finance? (Source of Annual Income) From Agriculture ☐ From Trade ☐ From monthly salary ☐
Other (specify) _____
- 3) Do you have saving in OMFI before getting loan? Yes ☐ No ☐
If your answerer is “yes” how much _____
- 4) For what purpose do you save?
a. To expand business ☐ d. For acquisition of Agricultural inputs like, fertilizers ☐
b. For Household consumption ☐ e. for participating in MSE program ☐
c. To pay school fees ☐ f. others(specify) _____
- 5) Why do you borrow from Omo microfinance?
To repay other debts to improve or expand business ☐ to open a new enterprise ☐
To purchase agricultural inputs ☐ improve the quality of existing products ☐
other (specify) _____
- 6) Do you believe the loan issued timely? (Less than 1 month timely otherwise not)
Yes ☐ No ☐
- 7) If your answers to #20 ‘No’ how do you evaluate the loan procedure time used by OMFI?
Too long ☐ medium ☐ Short ☐ Very short ☐
- 8) How much money did you receive in loan from Omo microfinance?
Round 1 ☐ Round 2 ☐ Round 3 ☐ Above around 4 ☐
- 9) Was the loan size you obtained from OMF sufficient to undertake for the purpose intended?
Yes ☐ No ☐
If your Answer is ‘No’ what was the amount you requested? Birr _____
- 10) The loan size you obtain from OMF is:- Too small ☐ Small ☐ Large ☐ Very large ☐
- 11) If your answer for #10 loan is too small or small what solution do you take?
Borrow from informal financial sectors (*Iddir* or *equb*) ☐ Borrow from formal banks ☐
Borrow from relatives and family ☐ Others (specify) _____
- 12) Do you spend the entire loan for running your business according to loan agreement?

Yes ☐ No ☐

13) If your answer to #12 is 'No' for what purpose you spent? (Multiple answers are possible)

For house hold consumption ☐ for health Care ☐ for wedding ceremony ☐

Other (specify) _____

14) Did you repay loan to OMFIs? Yes ☐ No ☐

15) If your answer to #14 is 'yes' what is your repayment status?

A. Fully repaid: on time ☐ too late ☐

B. Partially repaid: on time ☐ too late ☐

16) If your answer to #14 is 'yes' what motivates you to repay your loan on time?

- To keep social status in the expectation of getting another large loan ☐
- Build good relationship with the loan provider ☐ others (specify) _____

17) If your answer for #14 is 'No' what cause your repayment problem?

Weak legal enforcement for defaulters ☐ Loan activity was not profitable ☐

Personal problem (like sick, change of place) ☐ Lack of sale/ demand ☐

Low supervision by the loan officer of OMFIs ☐ Disaster (theft, fire, flood etc.) ☐

Used enterprise capital for consumption (food, clothing, HH goods) ☐

Family celebration (wedding, birth, etc.) ☐

18) Is the repayment period set by OMFIs suitable in your opinion? Yes ☐ No ☐

19) If your answer to #18 is "No" what do you think is the suitable repayment period?

20) Is the frequency of collection offered by OMFIs is suitable in your opinion? Yes ☐ No ☐

21) What was your preferable collection period? Weekly ☐ monthly ☐ quarterly ☐

semiannually ☐ annually ☐ other specify _____

22) Have you ever been supervised regarding loan utilization by OMF staff/officers?

Yes ☐ No ☐ If your answer is 'No' please move to Q. #24

23) Do you consider supervision as being important for loan repayment?

Yes ☐ No ☐ Do not know ☐

24) Interest rate for credit set by Omo microfinance is:

High ☐ Medium ☐ Low ☐

Part III:- Information On Group Lending Related Questions

1. When did you 1st join OMFIs? Month_____/year_____.E.C.

2. Why did you engaged in group borrowing?
 Easy to get loan in a group by initiation of one of the group members ☐
 By lacking other alternatives others ☐
3. How many members does the group in which you belong have?
 4-6 ☐ 7-10 ☐ above 10 ☐
4. How was the group formed? Based on the group member interest ☐
 Based on the loan provider (OMFIs) interest ☐ based on your comminute interest others ☐
5. During screening did you know about the behavioral integrity of all group members?
 Yes ☐ No ☐
6. If your answer in Q.#5 is 'No' you did not know your group member very well or did not know him/her at all, why did you accept him/her as a member in the group? ☐
 He/she is a friend of another member ☐ His/her business looks good ☐
 He/she is a relative of another member ☐ Other (specify) _____
7. Have you ever participated in another group? Yes ☐ No ☐
8. Do you think, you have responsibility to other members of your group related to loan repayment? Yes ☐ No ☐
9. What actions would you take when the group members didn't repay their loan?
 Moral persuasion ☐ Village gossip ☐ Hassling ☐ Exclusion from social activities ☐
 Others (specify) _____
10. Do you have livestock currently? Yes ☐ No ☐
11. Did/do you've your own land? Yes ☐ No ☐
12. If yes, how many hectares? Cultivated land_____ hector uncultivated land____hector.

PART IV:- Business Related Questions

- 1) In which Business activities currently you engaged?
 - Agricultural sectors (Like farming, poultry, dairy farm, animal fattening etc) ☐
 - Commercial/Trade/retail/activities Service sectors ☐ others (specify) _____
- 2) In Q#1, if you involved in Agricultural sectors, in which business activities you involved?
 Animal fattening ☐ bees farming ☐ crop production ☐
 Other (specify) _____
- 3) In Q#1, if you involved in enterprise sectors, in which business activities you involved?
 Constriction ☐ woodwork and metal work ☐ "Kobil" stone ☐
 Other (specify) _____

4) In Q#1, if you involved in service sectors, in which business activities you involved?

▪ Barber and beauty salon ☐

▪ computer maintenance and copy service ☐

▪ other (specify) _____

5) From above business activity you selected, how long have your business experience?

One year ☐ two years ☐ three years ☐ more than four years ☐

PART V:- Other General Questions about Omo Microfinance

1. What is your overall opinion about OMO microfinance institution?

2. If you face any difficulties and challenges during the repayment process, please mention. The major challenges you faced (internal as well as external) in loan repayment.

Thank you for your participation!!!