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A SENIOR RESEARCHPAPER SUBMITTED TO THE DEPARTMENT OF ACCOUNTING AND FINANCE IN PARTIAL FULFILMENT OF THE REQUIREMENT FOR BA DEGREE IN ACCOUNTING AND FINANCE

ASSESSMENT OF FACTERS AFFECTING LOAN REPAYMENT PERFORMANCE IN COMMERCIAL BANK OF ETHIOPIA IN WOLKITE BRANCH.

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AbbreviationsandAcronym

(CBE),CommercialBankofEthiopia.
(NBE),NationalBankofEthiopia

ABSTRACT

The main objective of this study is found out to the assessment of factors affecting Loan repayment performance in case of commercial bank in wolkite branch. The relevant data for this study collected from primary sources. To collect primary data by employees on judgemental types of questionnaire used. The collected data effectively Analyzed and presented by using percentage and tabulating.

This study had found that existence of competitors, market fluctuation, high interest rate and high limitation on providing loan are the main factors. The data for these factors was collected from commercial bank. this study will try to cover the repayment aspects of CBE in Wolkite branch and focus on the loan-related factors (for instance, loan reputation, Loan size, credit monitoring, collateral, credit term) affecting loan repayment performance of individual borrower.

Table of Contents

CHAPTER ONE

NTRODUCTION

1.1 Background of the study

A loan is when you receive money from a friend, bank or financial institution in exchange for future repayment of the principal, plus interest. The principal is the amount you borrowed, and the interest is the amount charged for receiving the loan. Since lenders are taking a risk that you may not repay the loan, they have to offset that risk by charging a fee - known as interest. Loans typically are secured or unsecured. A secured loan involves pledging an asset (such as a car, boat or house) as collateral for the loan. If the borrower defaults, or doesn't pay back the loan, the lender takes possession of the asset. An unsecured loan option is preferred, but not as common. If the borrower doesn't pay back the unsecured loan, the lender doesn't have the right to take anything in return. Study.com, (2019)

Regardless of type, every loan – and its conditions for repayment – is governed by state and federal guidelines to protect consumers from unsavory practices like excessive interest rate. In addition, loan length and default terms should be clearly detailed to avoid confusion or potential legal action. Now a day's there is a number of governmental and private owned banks in Ethiopia that providing loan for various purposes. But most banks financial Statement shows that the collections of loans from borrowers are not satisfactory. This result a huge amounts of non-performing loans NBE ,Annual Report,(2012)

Loans taken from credit institutions vary from country to country, region to region, sector to sector. However, credits of developing countries were found to share one common characteristics suffer from a considerable amount of default rate (the amount of loans not collected on current and past due loans for the reference periodKashuliza A, (1993).

There are many socio economic and institutional factors influencing repayment rates. Lending institutions are faced with four major problems in the course of undertaking credit activity,

A. To ascertain what kind of risk the potential borrower is (adverse selection)

B. To make sure the borrowers will utilize the loan properly once made; so that they will be repay it (moral hazard).

C. To learn how the project really did, in case the borrowers declares his inability to repay and

D. To find methods to force the borrowers to repay the loan if the borrower is reluctant (hesitat) (enforcement)Ghatak,Maitreesh&GuinnaneTimoth,W, (1999) Therefore, this study will try to pay attention to this sector of the economy by identifying the factors affecting loan repayment performance of commercial bank of Ethiopia in its wolkite branch.

1.2 Back ground of the Organization

Modern banking system in Ethiopia begun in 1906 with establishment of the bank of Abyssinia in Addis Ababa, It has fully foreign owned and also it has a door to introduce banking system in the country its aim is for profit making and motive for promoting banking systems.

It was liquidated and replaced by the bank of Ethiopia in 1931 and the Ethiopian government has a 60% owned and transactions were subject to the control of ministry of finance and economy and at the same time it opened branches in different areas.

In 1936 during Italian invasion the Italian banks were operating and the Italian banks notes formed the legal tender. After the Italian evacuated from our country in 1943 the state bank of Ethiopia was established. The bank at its establishment it has two departments performing the function of issuing and introduction of monetary and banking proclamation.

The commercial bank of Ethiopia is a public-owned financial service provider institution headquartered in Addis Ababa. The bank was founded in 1942 and named "State Bank of Ethiopia". It introduced saving and new currency, and opened 21 branches, including branches in Khartoum and Djibouti. In1963, the bank assumed the current name Commercial Bank of Ethiopia (CBE). Moreover, it abandoned the role of a central bank and maintained commercial bank functions.

1.3 Statement of the problem

Banks in many developing countries hold a truly alarming volume in non-Performing Assets Fry M, (1995). Given the fact that banks depend to the greatest extent on performing loans for their revenue, unmanaged or high levels of non-performing loans may precipitate the collapse of not only one bank but also the entire banking system and the economy (Waru&Kalani, 2009). Differences between promised and actual repayments are the result of uncertainty concerning the borrower's ability or wiliness to make the repayments. When they are due which are creates the risk of borrowers Default.(pischke,1991:vigano, 1993;kitchen,1989) .The banking sector in Ethiopia is at its infant stage, it has been facing various challenges and constraint. One of the

biggest challenge was management of nonperforming loans. The soaring loan achievement of repayment performance may have adverse impact on the financing performance of the bank as well as the progress of the economy.(wondimagengehu,2012. The probability of regular repayment depends on objective factors relating to the borrower's operating environment, the borrower's personal attitude towards loan obligation, and the bank's ability to evaluate these two aspects through the information it has and control credit risk specific contractual condition.
As mentioned above, various studies were conducted on the determinants of loan repayment performance in different countries. Most of these studies were focused on the credit associated with agricultural activities and they identified the socio-economic factors that affect the loan repayment rate of rural household based on taking sample from the beneficiaries.

Therefore, the study will try to assess factors affecting loan repayment performance focus on commercial bank of Ethiopia in Wolkite branch based on taking a data from employees of the bank.

1.4 Research questions

The study specifically will try to answer the following question

- How to assess effect of collateral on loan repayment performance?
- How to assess the significance of monitoring borrower's business on loan repayment performance?
- What are the effects of loan monitoring on loan repayment performance?
- How to assess the influence of huge loan on credit default?
- How to assess the impact of credit term on loan repayment performance?

1.5 Objectives of the study

1.5.1 General objectives

The general objective of this study is to identify loan related factors that affecting loan repayment performance by CBE in Wolkite branch.

1.5.2 Specific objectives

- To assess the effect of collateral on loan repayment performance.

- To assess the significance of monitoring borrower's business on loan repayment performance.
- To assess the effect of loan monitoring on loan repayment performance.
- To assess the influence of huge loan on credit default.
- To assess the impact of credit term on repayment performance.

1.6 Significance of the study

One of the key factors for profitability and sustainability of lending institutions is the presence of good loan repayment rates. There are a number of socio economic, lenders and loan related factors that affect the loan repayment rates. Weinberg, J.A, (1995) Analyzing such factors and create an appropriate solution are essential to expand the activities of these financial sectors in a sustainable manner. The primary advantage of the study is to establish a knowledge that enables to sound decision and to take corrective action. In addition, the information will be useful for policy makers to formulate successful credit policies and programmers that enable them to allocate scarce financial resources to the development of basic sectors of the economy and other lending institutions. Regarding CBE there has not been any empirical research conducted to identify the main causes of high default rates and to design future strategies. This study will try to provide information for a better understanding on the factors affecting loan repayment performance of the CBE from both the lender and borrowers side.

This study will serve the researcher to extend the scope of knowledge about the problem raised above. In addition to the advantages to the policy makers, programmers, decision makers and researchers this study will provide a basis to other researchers to use it as a reference.

1.7 Scope of the study

The area of the study will be focused on CBE in Wolkite branch. it established in 24/09/1973 E.C.The special scope of the study will be delimited to assess only the factor affecting loan repayment performance in case commercial bank of Ethiopia in Wolkite branch. There are many factors affecting bank's efficiency and effectiveness in achieving its goals and objectives. Such as, loan management, repayment performance, cash management and so on. Due to the nature of the research it could be very difficult to cover all the factors affecting loan repayment performance in commercial bank of Ethiopia in Wolkite branch. But this study will try to cover the repayment aspects of CBE in Wolkite branch and focus on the loan-related factors (for instance, loan reputation, Loan size, credit monitoring, collateral, credit term) affecting loan repayment performance of individual borrower.

1.8 Limitation of the study

The study will be face various limitations such as

There is no way to evaluate the reliability of the expert or authority in purposive sampling,

Qualitative type of data has limitation; dependent on skills of the researcher particularly in the case of conducting interviews and collection of qualitative data is generally more time consuming than quantitative data collection, it is generally necessary to include a smaller sample size.

Questionnaire method is primary used to gather primary data. However, different respondent interpreted questions differently, questionnaire do not provide an opportunity to collect additional information and the information may not free from personal bias of respondent,

Relative to structured interview – no rich data, all anticipated, the quality of data is depending on the quality of interaction and time consuming.

Primary source data also has limitations, primary data is not immediately available – takes time to define problem and not as readily accessibl

CHAPTER TWO

LITERATURE REVIEW

In this section the review of related litterateurs are presented. It starts on the theoretical foundation of the study. Subsequently types of loan or credit, the relationship between lending and credit repayment performance, and factors of loan repayment performance are also presented respectively. At the end empirical evidence that show the determinants of loan repayment performance in Ethiopia and outside the country is also presented.

2.1 Theoretical literature reviews

This part of the paper will provide a closer look on theoretical foundations and contributions on the subject matter. A bank exist to perform a number of functions chiefly, accepting deposits and granting credit (loans and advances) categorically provided as primary or banking functions. In fact banking means accepting for the purpose of lending of investment of deposits of money from the public, Granting of credit facilities by commercial banks which is the primary function as pointed out earlier, expose them to credit risk. Credit is a Device for facilitating transfer of purchasing power from one individual or organization to another.

Promises are frequently broken and there may be no objective way to determine the likelihood that promise will be kept Dwight &Stiglitz, (1990). Banks in many developing countries hold a truly alarming volume in non-performing assets. Differences between promised and actual repayments on loans are the result of uncertainty concerned the borrower's ability or willingness to make the repayments when they are due which creates the risk of borrowers default pische, 1991; vigano, (1993); kitchen, (1989)

There are those who argue that failure of lending agencies playing their roles in loan disbursement and recovery process is a major contribution to loan defaultOkorieAja and Andrew eheanacho,(1992); Vigano,(1993); Fry, (1995), (1992).

A mistake on the evaluation of the borrowers' characters or the introduction of inappropriate loan conditions may increase the total risk of the transaction Vigano.L (1993).Fry M (1995) listed bank lending criteria in east Africa in order of importance to show the method of credit analysis is weak: first the securities offered, second any other additional securities, third how short the period to maturity is, fourth the commissions to receive in connection with the granting of credit, fifth the amount and sixth the project.

2.1.1 Types of loan or credit

Bank loan have a conquered, and as at present, hold, many different collection of obligations. Some are productive some are to be repaid in a lump sum and other in installments.

Nothing definite about the maturity of loans is indicated purpose wise; loan may be classified in to commercial and industrial, agricultural, areal estate, consumers and other depending up on the use loans are secured and unsecured depending up on the facts weather collateral have been deposited against theme or no Richard, (2012).

2.1.2 Relation between lending and credit repayment performance

One of the primary objectives of financial institutions is to provide financial service (credit and saving) to people, in order to release financial constraints and help alleviate poverty.

Each financial institution tries to maximize its repayment performance whether or not it is profit oriented (Han.2008), High repayment rates are indeed largely associated with benefit both for the financial institution and the borrower. That enable the financial institution to cut the interest rate it charges to the borrowers, thus reducing the financial cost of credit and allowing more borrowers to have access to it Kion&Story, (2003). Improving repayment rates might also help reduce the dependence on subsidies of the financial institution which would improve sustainability. It is also argued that high repayment rates reflect the adequacy of financial institution services to client's needs. Related also repayment performance is akey variable for donors and international funding agencies on which many financial institution still depend for their access to funds. The first-best level of repayment performance is aperfect (100%) on-time repayment rate Ongena&David,(2001).

Such strategies include the allocation of larger loans to borrowers with lower default probability and attempt to reduce the delay in repayment. The financial institution will develop incentive mechanisms so as to meet these objectives. The main factors influencing repayment are either related to institution asymmetries, to adverse shocks affecting the borrower or to the low performance of institution Elsas&Krahen, (2000.)

Information asymmetries arise when gaining information on the characteristics or on the behavior of the borrower are costly for the financial institution. information asymmetries generate problems of adverse selection, allocation of loans to borrowers with undesirable characteristics such as a high level of riskor in ability to take advantage of the loan as well moral hazard the borrower may be have in an undesirable way (make little or insufficient effort to take advantage of his loan or used it for unproductive purposes Lown& Morgan, (2003). Adverse selection and moral hazard increase the proportion of borrowers also cannot repay their loans on time.

Borrowers that have enough money to reimburse their loan might also default strategically. The cost of strategic default might indeed below if the lending institution has low collateral requirements and if the legal system gives little power to the financial institution to enforce contracts. Financial institutions try to restrict the occurrence of those three types of situations in designing appropriate credit schemes.

Screening and monitoring procedures gives an information advantage to banks that allow them to overcome information and incentive Problems between the bank and the borrower. Therefore, the main benefit attributed to bank financing with respect to other sources of finance is that banks help overcome problems of asymmetric information by producing and an analyzing information and by designing loan contracts that improved borrower's incentives. Bank financing may also need some costs.

Degryse&Cayseele (2000) develop a model of loan pricing in which firms be a research costs to find a new bank. They show that loan rates offered by the relationship bank are higher than those offered at competing banks, because the latter are willing to offer an interest lower than their funding cost in order to capture the firm. The critical assumption in that model is the existence of exogenous search costs. In the early nineties, two influential papers warned about the potential costs of bank lending even when there are no exogenous costs of starting a relationship. Elsas&krahen, (2000) present a model in which relationship arises endogenously. A bank that lends to a formal earns more about that borrower's characteristics than do other banks.

This generates an asymmetry of information among banks. Therefore, a distinction is made between relationship (informed) banks and transaction (uninformed) banks. Informed lenders can capture some rents generated by their older costumers. While the uninformed competitors face winner's curse problem. In a competitive world the implication for loan pricing is increasing interest rates with the duration of the relationship. In the model of Kano, Uchida, Udell&Watanabe (2006) a firm balances the costs and benefits associated to two borrowing sources, namely informed debt and arm's length debt. Bank debt is provided by an informed bank that monitors the firm and exerts some control on the owner's decision to continue a project only if it has positive net present value. Contrast, arm's length debt guarantees that the owner exerts the optimal level of effort but lenders do not have control over the owner's continuation decision.

2.1.3 Factors of loan repayment performance

According to), Babouck&Jancar (2005) there are exogenous factors to the banks that influence non-performing loan. However, Richardetal, (2012)observes that there are endogenous forces inherent in the banks institutional process influence the levels of non-performing loan. Loans and advances constitute the primary source of income by banks. As any business establishment a bank also seeks to maximize its profit. Since loans and advances are more profitable than any other assets, a bank is willing to lend as much of its funds as possible. But banks have to be careful about the safety of such advances. Bankers naturally try to balance the issue of maximizing profit by lending and at the same time manage risk of loan default as it would non–profit and there by the very capital. Thus a bank needs to be alert in advancing loans as there is a great risk which follows it in a situation where the loan is defaulted.

Generally, in developing and under developed countries, the reasons for default have different aspect. Various researchers have concluded various reasons for loan default. South western Nigeria The result showed that the number of visits made by loan officers to the borrowers, higher level of education, and time of loan disbursement would have a better repayment performance. Moreover, borrowers with lower number of household members would meet their repayment obligation better than those with high number of household members. And having access to business related information and providing training to the clients are increasing the loan repayment rate of the borrowers.This literature categorizes factors of loan repayment performance. The following elements show that the factors of non-performing loans.

2.1.3.1 High Interest Rate

Banks that charge high interest rate would comparatively face a higher default rate or non-performing loans.

2.1.3.2 Loan Reputation

The borrower is repeated one he may have acquired more experience on the banks rules and regulations, hence could efficiently utilize the loan for the intended purpose. Therefore, a negative sign is expected.

2.1.3.3 Collateral

Collateral (also called security) is the assets that the borrower pledges to the bank to mitigate the banks risk in event of default. It is something valuable which is pledged to the bank by the borrower to support the borrower's intention to repay the money advanced. It is the lender secondary source of repayment or security in the case of default. Having an asset that the bank can seize and liquidate when a borrower's default reduces loans, but it does not justify lending proceeds when the credit decision is original made.

The formal credit analysis procedure includes a subjective evaluation of the borrower's request and details review of all financial statement. The initial quantitative analysis may be performed by credit department employees for the loan officer (seifu, 2002).

2.1.3.4 Loan monitoring

Lending decision is made on sound credit risk analysis /appraisal and assessment of credit worthiness of borrower. But past records of satisfactory performance and integrity are no guarantee future, though they serve as useful guide to project trend in performance. Loan granted on the basis of sound analysis might go bad because of the borrower may not meet obligation per the terms and conditions of the loan contract. It is for this reason that proper follow up and monitoring essential. Monitoring or follow up deals with the following vital aspects:

- Ensuring compliance with terms and conditions
- Monitoring end use of approved funds
- Monitoring performance to check continued viability of operations
- Detecting deviations from terms of decision.

2.1.3.5 Term loans

Term loans are credit facilities availed with an agreement to pay back the principal with interest within a specified period of time i.e. due date of final settlement set in advance. Loan settlement arrangements are made by way of periodic installment that can be programmed on a monthly, bimonthly, quarterly and semiannually or lump sum depending on the cash flow. Term loans are classified as short, medium and long term.

2.1.3.5.1 Short Term loans

Short term loans are facilities availed for a maximum period of 18 months for working capital purpose. End use of short term loan granted should be effectively followed by visits made to business sites and evaluation of the financial standing of the borrower both before and after disbursement of loan.

2.1.3.5.2 Medium Term loans

Medium term loans are granted for the purchase of capital goods, trucks, trailers, public transport, buses or investments whose pay back periods are justified. Duration of medium term loan can extend up to a maximum period of 60 months.

2.1.3.5.3 Long Term Loans

Long term loans are loans granted for the financing of business of investment nature. The financing includes participation in the establishment of viable business ventures and supporting expansion program of successful business. Manufacturing, mining, and building and construction sectors are among the beneficiaries of long term loans. The duration of long term loans extends up to ten years.

2.1.4 Identification of potential customers

For effective management of credit, banks and other institution do not extend their credit service to all credit requests but theyanalyze the request from different angles. The firm need not follow the policy of treating all customers equally for the purpose of extending credit. It requires adequate information system at a regular interval for ensuring the selection of potential customers who are capable of repaying the credit and service charge and safeguarding bank interest against uncollectable risk. To identify these potential customers, it is necessary to collect credit information, analyze it, and reach the final decision (Zaman, 2000 and Khandkher, 1998).

2.2 Empirical literature reviews

As indicated by Oyatota,(1983) (vo1s.7,) credit provides the bases for increased production efficiency through specialization of functions thus bring together in a more productive union the skilled labor force with small financial resources and those who have substantial resources but lack entrepreneurial ability.

As Nugyen, (2007) considers, a model of repeated moral hazard without learning and risk neutrality. In the optimal loan contract, the loan interest rate and collateral requirements decrease with the duration of the bank-borrower relationship, after the firm has demonstrated some project success. In a recent contribution, Freixas (2005) presents amodel where relationships arise because there is an initial fixed cost of monitoring, that is, the loan interest rate in the second period is larger than in the initial contract in the models of On gena&Smitht, (2001) predict that interest rate increases with the duration of the relationship. In contrast, the model of Orebiyi,(2002) show that interest rates should decline as relationships matures. Finally, some authors argue that loan rate smoothing arises as part of an optimal contract between borrowers bank firm relationship.

Studies in Ethiopia

Berhanu A, (2005) studied on the determinants of loan repayment performance of small holder farmers in north Gondar, Ethiopia. A total of 17 explanatory variables were considered in the econometric model. Out of these seven variables were found to significantly influence the repayment Performance.

Abafita (2003) Analyze the micro finance repayment performance of Oromia credit and saving institution in kuyu, Ethiopia. According to his finding sex, loan size and number of dependents are negatively related to loan repayment. On the other hand age was found to be positive, while age squared turned to be negative. Income from actively related to loan repayment period suitability and loan supervision are significant and negatively related to loan repayment performance. Moreover, loan diversion is significant and negatively related to loan repayment performance. The negative sign implies that the use of diverted funds for non-income generating purposes.

Assefa (2005) estimated the effects of hypothesized explanatory variables of 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.

AbrehamG. (2002) studied on the loan repayment and its determinants in small-scale enterprise financing in Ethiopia around zeway area. He is found out other source of income, education, and work experience related economic activities before the loan are enhancing loan repayment. While extended loan repayment period is influence the repayment performance negatively.

2.3 Conclusion and identification of knowledge gap

As mentioned above, various studies were conducted on the factors of loan repayment performance in different countries. Most of these studies where focuses on the credit associated with agricultural activities and they identified the socio-economic factors that affect the loan repayment rate of rural household taking sample from the beneficiary, however, in the literature review nothing was indicated about the bank internal factors influencing the loan repayment performance. Thus, this research could focus on the by taking the sample from the bank employees.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1. Research designs

A research design will provide relevant information that was most efficiently and effectively address the research question or hypotheses. The study was tried to adopt descriptive type of research design this is because the objective of the study is to describe the effect of loan repayment performance of customers. Study approach qualitative data approach has used for the study.

3.2. Target Population

The target populations of the study are employees of the banks who currently accessed loan provision and are in process of repayment. The population sizes of the study are 24 employees of CBE in Wolkite branch. In this cause to fill the gap that most previous researchers were studied based on the sample taking only from borrower's side. But, this study will conduct only from employees of CBE in Wolkite branch.

3.4. Types and source of data

To collect the necessary data the study was used primary source of data.

Primary data – the study was tried to use primary source of data which are qualitative in nature only which will be collect from the employees of the organization (loan creditor or credit manager) by distributing questionnaire and interview through related parties.

The study was used structured interview – fixed list of questions only we can use steer the conversation. And the study was use employees judgemental type of questionnaire.

Qualitative data - the study was used qualitative data type, which is represented by a name, symbol, or a number code.

3.5. Method of data analysis

After collecting all necessary data from primary data sources the study tries to be analyzes the collected data by using descriptive type of data analysis in which the results have been present and analyze by using tables and percentages.

CHAPTER FOUR

4.1 DATA PRESENTATION AND ANALYSIS

In the previous chapter, the overall methodology, which was focused on research purpose, research approach, research strategy and the specific method of data collection and data analysis used in the study, has been presented. On the other hand, this chapter presents the results and analysis of data collected via questionnaire. The survey results of this chapter are organized as, the first section presents background information of the respondents, second section factors affecting loan repayment and the third section presented the result of credit related departments response.

The questionnaire was distributed to the employees (credit related professionals). It was physically distributed to 15 employees of the bank. Out of 15 questionnaires 15 were completed and collected. As a result the response rate was 100 percent.

Table 4.1 survey response rate

Sample size	Frequency	Percentage
Completed and returned questionnaires	15	100%
Total	15	100%

4.2 Back ground information of the respondents

Table 4.2 Respondents sex

Sex	Frequency	Percent
Male	9	90
Female	6	60
Total	15	150

Source: Survey outcome:2015

According to the survey result 90% of the respondents were males and the rest of 60% were females.

Table 4.3 **Respondents experience in the bank**

Years of experience	Frequency	Percentage
Less than 1 year	0	0
1 up to 5 years	2	20%
6 up to 10 years	7	70%
10 up to 15 years	1	10%
Total	10	100%

Source: Survey outcome: 2015

. In this case 20 percent of respondents had 1-5 years' experience in bank credit process while70 percent had an experience for 6-10 years. 10 percent of respondents had more than 10 years' experience. 0 percent of the respondents had less than one-year experience The fact that majority of the respondents had many years' experience in bank credit operation helped capture a good quality of data.

4.2 Factors affecting loan repayment

The study tried to assess the factors that affect loan repayment performance in the context of commercial bank of Ethiopia in Wolkite branch. The study required respondents to show their agreement or disagreement to certain statements dealing with loan factors cause occurrences of loan default.

Table 4.4 Factors indicating interest rate and loan default

The bank Employees responses	Strongly agree %	Agree%	Neutral %	Disagree%	Strongly disagree%
Loans with big interest rate may cause loan default	0	5 0	0	4 0	1 0

Source: Survey outcome: 2015

Table 4.4 above, indicates that 50% of the respondents agree with the statement that charging higher interest leads to loan default. On the other hand, 40% of the respondents disagree that charging high interest rate leads to loan default. Among the respondents 10% the response is strongly disagreeing with the question.

Banks that charge high interest rate would comparatively face a higher default rate or non-performing loans, Study by (Nkusu M. 2012) described that high interest rates result in deterioration of borrower's repayment capacity and hence, cause nonperforming loan. Study by (Waweru&Kalini, 2009) on the commercial banks in Kenya using statistical analysis indicates that high interest rate charged by the banks is one of the internal factors that lead to incidence non-performing loans. A study conducted by Espinoza and Prasad (2010) on Greece banking system shows higher interest rate increase the loan default rate.

This shows that as the cost of capital (interest rate) is high, the borrower's responsibility will be also high to pay the principal plus interest at the maturity date; as a result, they may face loan default.

Table 4.5***Relation between materializing loans and occurrence on loan default***

The bank Borrowers responses	Strongly agree %	Agree%	Neutral %	Disagree%	Strongly disagree%
Internalizing loans helps to protect loan default?	10	90	0	0	0
Low collateral requirements has lower loan repayment performance	0	50	20	30	0
Most of the time non-collaborated loans are defaulted	10	50	0	40	0

Source: Survey outcome: 2015

Survey result of the study shows that 90% of the respondents agree on the statement of collateralized loans help to protect loan from default. On the other hand, 50% of the respondents agreed that low collateral requirement has lower loan repayment performance and 50 % of the respondents agreed that most of the time non collateralized loans are defaulted.

Collateral (also called security) is the assets that the borrower pledges to the bank to mitigate the bank's risk in event of default (Sinkey, 2002) Security is taken to mitigate the bank's risk in the event of default and is considered as a secondary source of repayment (Koch TW & Scott MacDonald, 2003).

Therefore, according to the study the researcher understands that, since the borrower's property (such as home or vehicles) pledged as collateral that have to be sold if the borrower defaults and has no other way to repay the lender, they repay the loan with compliance to the agreement as well as collateralized loan (security) is used to reduce the risk of giving credit by increasing the chances of the lender recovering the amounts that become due to the borrower.

Table 4.6***factors indicating credit monitoring and loan default***

The bank employees response	Strongly agree %	Agree%	Neutral %	Disagree%	Strongly disagree%
Strict monitoring of borrowers business ensures good loan repayment performance?	7 0	3 0	0	0	0
effects of loan monitoring on loan repayment performance	2 0	4 0	3 0	1 0	0
Poorly accessed loans may perform well if proper credit monitoring applied?	0	4 0	0	5 0	1 0

Source: Survey outcome: 2015

Accordingly, 70% of the respondents agreed on giving regular attention on borrower business activity reduces the loan default rate.

A bank can use different ways to monitor the borrower. Follow up the financial stability of a borrower can be done by periodically examining the operations of the accounts, examining the stock statements and ascertaining the value of security. Visiting the borrower periodically to have understanding of the progress of the borrower’s business activity and thereby give advice as necessary is also among the methods banks adopt to follow up their loans.

The loans are more secured if the banks keep a continuous check on the borrowers. The bank need to give their borrowers full attention, so they are not relaxed at any stage about repayment of their loans. It has been seen that less monitoring of borrowers lead to non-performing loan (Agresti,2012). This indicates that, if the banks monitor their borrower's property, and give due attention to the borrowers and what they are doing with the money and then recognize warning signs early enough, there may be a tendency by borrowers to give better attention to their loans when they perceive they got better attention as a result the borrowers are on the position of good performance to repay the loan. (Retta 2000) employed probity model for loan repayment performance of women fuel wood carriers in Addis Ababa. His finding is frequency of loan supervision are found to be encourage repayment hence reduce the probability of loan default.

As (Farhan, et a1. 2012) recommended, close monitoring of the borrower business activity gives the bank an opportunity to evaluate the borrower's ability to pay the loan. According to the survey result, higher budget for loan monitoring reduces loan default believed to ensure loan performance by 4 percent of the respondents. In another way only 50% of the respondents disagreed poorly accessed loans may perform well if proper monitoring applied. This indicates that follow up may not substitute credit analysis or assessment; On the other hand, only 40% of the respondents agreed on the statement that banks with higher budget for loan monitoring have lower non-performing loans. Though loan monitoring requires budget, allocating higher budget might not ensure loan performance as a small number of respondents are neutral to this assertion.

Table 4.7 Factors indicating loan amount, Credit terms, and loan default

The bank employees response	Strongly agree %	Agree%	Neutral %	Disagree%	Strongly disagree%
High loan amount leads to large default rate	0	6 0	2 0	2 0	0
Poorly negotiated credit terms lead to loan default	0	8 0	0	2 0	0
Having large number of borrowers causes loan	0	2 0	0	7 0	1 0

Source: Survey outcome: 2015

According to the survey result 60 % of the respondents agreed on the statement that deals with the amount of loan that is greater or lower than the borrowers has been requested amount would result in loan default.

On the other hand, 70% of the respondents were disagree on the statement of having large number of borrowers causes loan default

If the amount of loan exceeds what the borrower needs and can handle, it will be more of a burden than help and extra funds may go toward personal use (Norell, 2001), thereby undermining repayment performance. If the loan is too small, it may also encourage borrowers to divert the loan to other purposes.

. From this result the researcher gains knowledge of large number of borrowers may not lead to loan default because it is essentially depend on the ability of the lender to monitor regularly and other factors which argue above such as, interest rate, loan amount, credit term and so on.

Table 4.8 Factors indicating Training, Loan reputation, credit term and loan default

The bank employees responses	Strongly agree %	Agree%	Neutral %	Disagree%	Strongly disagree%
Training borrowers regarding the bank rules and regulation has a positive impact on loan repayment?	4 0	5 0	1 0	0	0
Loan default become low if the borrowers are repeatedly borrowed?	1 0	6 0	2 0	1 0	0
Does credit term an effect on loan repayment performance?	2 0	7 0	0	1 0	0
Long term credit have higher tendency of repayment?	1 0	5 0	1 0	3 0	0

Source: survey outcome 2015

As shown table 4.8 above all of the respondents were agreed on misunderstanding of the borrowers about the credit terms is the cause of nonperforming loan. In the same manner, No one respondent were disagree with training about the rule and regulation of the loan is contributed for high repayment performance rate. The study also shows 70% of respondents agree with credit terms have an effect on loan repayment performance and 50% of the respondents agree with long term credits have higher tendency of repayment (low loan default) and only 30% of them disagree with the idea.Similarly, the survey result shows 60% of the respondents agree with the loan default become low if the borrowers repeatedly borrowed.

Training is one of the important requirements for the success of microfinance institution (Assefa, et al, 2005) they also develop skill on how to do business and money utilization. Training is needed not only for clients but also for loan officers. In both case it has a positive contribution to the repayment rate. (Norell D. 2001) Also agree on the importance of training for the decreasing of default rate.

As it had been indicated by (Rose, 2002; Koch & McDonald, 2003) a borrower has built up a good reputation or credit record if past commitments were promptly met (observed behavior) and repaid timely. As understood from this, the borrower is repeated one he may have acquired more experience on the banks rules and regulations, hence could efficiently utilize the loan for the intended purpose.

Therefore, this study gains knowledge of if the lender provides various training, the clients will able to understand the rule and regulation easily, which provides that the framework for lending and guide the credit-granting activities of the bank. As a result, they were not failing to repay loan in accordance with the terms of the lender.

4.3 Loan related professional response

Know your customers (KYC) policy of the bank leads to high repayment performance

An issue of knowing the customer, customarily known as KYC (Know Your Customer) is so vital before proceeding to details. Banks use various means to obtain such information about the existing or potential customer. Use of financial statement, credit report from credit bureau, customers' history if not new is the potential sources of information (Ross et al., 1998). In fact, the exchange of credit information improves non-performing loan ratios, leads to fewer losses through write offs and decreases interest rates for good credit risks (Jentzsch, 2008) further support as that sharing credit information between lenders intensifies competition and increases access to finance. So, indicates that all of the respondents accept the statement of know your customer (KYC) policy of banks lead to high loan performance, This result indicates that the exchange of credit information improves non- performing loan ratios.

4.4 Training loan officers about the external environment is important

Training is needed not only for clients but also for loan officers. (Norell D. 2001) agree on the importance of training for the decreasing of default rate. Study by (Kalini 2012) indicates lack of proper skill amongst loan officials, speedy process of evaluating loans mainly due to external pressure, are among the factors that lead to huge concentration non- performing loans. As the survey result of the study indicates that all of the respondents accept the statement that deals about the importance of training the loan officers regarding the external environment. Therefore, this study gains knowledge of if the bank provides various training to the loan officials about the external pressure it can reduce the rate of non-performing loan.

4.5 Challenges and difficulties during the loan repayment process

Respondents were identified the major challenges in the loan repayment process as follows,

- Significant number of borrowers do not repay timely.
- No training is given by the institutions.
- Fail to know the right customer for loan.
- Most borrowers have not enough knowledge about the amount of money they should be paid (misunderstanding of interest calculations).
- They are not know the exact due date of the loan
- Poor knowledge and experience by borrowers
- Whether condition issues
- Political instabilities
- Bankruptcy

4.6 The incentive mechanisms for borrowers who borrowed repeatedly

The sample respondents identified incentive mechanisms' used by their bank for prominent customers or borrowers. Among this:-

- Reducing the amount of collateral that the customer may offered,
- If the credit term passed, they will tolerate them up to someday.

Generally, almost all respondents had recommended that there are bank specific factors that affect the loan repayment performance. The study also found the above results for each of questions raised in relation to the factors which affect the loan repayment performance. Next to this conclusion and recommendation parts of the study are presented on the last chapter of the paper.

CHAPTER FIVE

5. 1 CONCLUSION AND RECOMMENDATIONS

5.2 Conclusion

The broad objective of this research was to identify credit related factors of loan repayment performance. Based on the broad objective a number of specific research questions were developed. To achieve this broad objective, the study used mixed research approach.More specifically study used employees judgmental questionnaire in order to obtain primary data from the target sample. The results showed that, based on the respondents' view it was evident that most likely factors that affect occurrences of loan default in Commercial Bank of Ethiopia in Wolkite branch are presented in the paragraphs that follow.

- The study indicates that training is one of the important requirements for the success of lending institutions. If the lender provides various training, the clients will able to understand the rule and regulation easily. They also aware of the terms of the credit and develop skill on how to do business and money utilization.
- The study also shows credit terms have an effect on loan repayment performance and long-term credits have higher tendency of repayment (low loan default).
- The respondents of the study also indicate the challenges and difficulties during loan repayment process such as poor knowledge and experience of borrowers, untimely repayment, external factors including whether conditions and political instability.
- on banks that charge high interest rate would face a higher default rate or non-performing loans.
- Besides, banks are not lend without any collateral to ensure the full commitment of the borrower, to provide protection if the borrower deviate from the planned course of action outlined at the time credit is allowed, and to provide insurance if the borrower default. However, lower collateral requested by the bank has a higher default risk.
- The banks monitor their borrower's property, and give due attention to the borrowers and what they are doing with the money and then recognize warning signs early enough. There may be a tendency by borrowers to give better attention to their loans when they got better attention this found to be encourage repayment hence reduce the probability of loan default. However, a bank can use different ways to monitor the borrower. Such as follow up the financial stability of a borrower can be done by periodically examining the operations of the accounts.
- This study also give you an idea that if the amount of loan exceeds what the borrower needs and can handle, it will be more of a burden than help and extra funds may go

toward personal use thereby undermining repayment performance. If the loan is too small, it may also encourage borrowers to divert the loan to other purposes.

- Negotiation about credit term would fail to indicate terms and conditions of loan properly, among others. This might mean loan disbursement might not be made timely; grace period may not be given properly, repayment amount set wrongly without considering the cash flow. Either of these or related would comparatively lead to poor loan performance.

- Finally, the study found that if the borrower is repeated one he may have acquired more experience on the banks rules and regulations, he could efficiently utilize the loan for the intended purpose and paid at the ordered time. With regard to this, the respondents also try to indicate some incentive mechanisms used by the bank for such prominent customers or borrowers, such as reducing the amount of collateral that the customer may offered.

5.3 Recommendations

After close examination and analysis of the research findings, the following recommendations are suggested: -

- Banks should reduce the rates of interest and allow their customers to return the money that they borrowed, since it is crucial to banks in making limited profit especially in situations where they would have made great losses.

- Since the offer of security influences the lender's decision whether or not to lend, and it also changes the terms on which he is prepared to lend, typically by increasing the amount of the loan, by extending the period for which the loan is granted and by lowering the interest rate. Bank should be giving more attention on the recording of borrower's property used as collateral. Therefore, if the borrower secures high valued collateral, they may feel that it will not be loss in case of loan default. As a result, borrower will be in a position to repay the debt.

- Banks should be made periodic assessment of the health of the loans. Some of the key indicators of performance that might include profitability, activity level and management of the unit. These ensure that the assets created are effectively utilized for productive purposes and are well maintained.

- Bank should be lending the amount of loan that is enough for the purposes intended, this means the amount of loan do not exceeds or small what the borrower needs and can handle.

Banks should be attention grabbing to provide training about the rule and regulation of the loan for their client. This is because of training is not only important for the borrowers to understand the rule and regulation easily and to develop skill on how to do business and money utilization, but also for loan officers. In addition to this, banks should accept more experienced borrower's while giving a loan, because they have a better awareness about the rules and regulation of the bank

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Appendix

Dear respondents: The questionnaire is designed to conduct data to be used as an input for the research entitled "Assessment of factors affecting Loan Repayment Performance a case Study on Wolkite branch. Dear respondent, I would like to thank in advance foryour help in filling this questionnaire and that your responses would be kept confidential.

Directions:-To fill this questionnaire, please, put check mark "√"to the choice and closed ended questions in the box and write your explanation for interview in the space provided in clear and precise words.

Questions filled by the bank employees'

Backgroundinformation

1.1.Sex: Male Female

1.2.Age: 18-22 23-27 28-32 >33

1.3.Marital status Married -

Unmarried

1.4.Educational status.

Diploma

First degree

Above degree

1.5.For how long you have been in the Bank.............................

Close end Questions

1. Charginghigh interest rate causes loan default.

A.Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

2. Collateralizing loans helps to protect loan default.

A. Strongly agree B. Agree C. Neutral D. Disagree E. strongly disagree

3. Low collateral requirement has lower loan repayment performance.

A. Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

4. Most of the time non-collateralizedloans are defaulted.

A .Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

5. Strict monitoring of borrower's business ensures good loan repayment performance.

A. Strongly agree B. Agree C. Neutral D. Disagree E. strongly disagree

6. High loan amount leads to large default rate.

A.Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

7. Poorly negotiate credit terms lead to loan default.

A .Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

8. Having large number of borrowers causes loan default.

A. Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

9. Training borrowers regarding the bank's rules and regulation has a positive impact on loan repayment.

A. Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

10. Loan default become low if the borrowers are repeatedly borrowed.

A . Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

11. Does credit term have an effect on loan repayment performance?

A. Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

12. Long terms credit have higher tendency of repayment.

A. Strongly agree B. Agree C. Neutral D. Disagree E. Strongly disagree

II.INTERVIEW

1.Know your customers (KYC) employee's policy of the bank leads to high repayment performance?

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____
____

2.Is training (The borrower have use the money appropriately)loan officers about external environment?

____
____
____

3. What are the challenges and difficulties during the loan repayment process?

4. What are the incentive mechanisms for borrowers who borrowed repeatedly?